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THE EVOLUTION OF OIL AND GAS LAW

*Maurice H. Merrill**

Try to explain the law to any intelligent layman, and you will find yourself compelled to speak in terms of a body of rules governing men and their affairs, enforced by the power of the organized society.[1] So much homage must we yield to the imperative theory of law held by the analytical jurist, now the target for stones from the juridical right[2] and left[3] alike. Nevertheless, we all realize that this does not tell the whole story. The habitual judicial technique,[4] the taught tradition[5] and the ideals of the end of law[6] all have their part to play in the determination of the body of rules and how they are to be used. Current scientific knowledge, the needs and the asserted desires of important components of the community, and the "voice of experience" concerning the operation of various rules and principles affect the course of legal development. Hence the law does not, as it cannot, stand still; and, in any of its realms, legislation and decision alike combine in a process which makes the corpus juris of today quite different from that of even a half-century ago.

The law as applied to oil and gas has had a checkered career since, in the first American case involving oil, the court defined that fluid as "a peculiar liquid not necessary nor indeed suitable for the common use of

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[1]See, for example, JENKS, THE BOOK OF ENGLISH LAW (1929) 7; STONE, LAW AND ITS ADMINISTRATION (1915) 3.

[2]POUND, FIFTY YEARS OF JURISPRUDENCE (1937) 50 HARV. L. REV. 557, 564, 570.

[3]FRANK, LAW AND THE MODERN MIND (1930) *passim.*

[4]Pound, *The Theory of Judicial Decision* (1923) 36 HARV. L. REV. 641, 646.

[5]See POUND, THE FUTURE OF THE COMMON LAW (1937) 8: "A system of law is essentially a taught tradition of ideals, methods, doctrines, and principles, continuous as long as the course of teaching remains unbroken. The common law is a system of this sort, a tradition of taught law, continuous in England from the establishment of an organized teaching in the Inns of Court to the decay of that teaching in the sixteenth and seventeenth centuries, and then, as remade in the age of Coke, continuous in the several lands of the English speaking world from the seventeenth century."

[6]POUND, AN INTRODUCTION TO LEGAL PHILOSOPHY (1922) cc. I, II.

man."[7] It is less than a century since the famous well of Drake and his associates launched the oil industry upon its checkered career.[8] In its course of development it has been subjected to the play of many and diverse influences. To practitioners in a state where the law is yet to be formulated, a survey of its evolution may be of more than academic interest, since it may afford a criterion by which to evaluate the authorities which they may find in the reports of other jurisdictions.

What were the conditions under which our courts were called upon first to apply the law to oil and gas? Here were substances to be won from the earth like other minerals by an arduous and costly process, beyond the skill or the financial resources of the average landowner. Of necessity, exploitation involved sale of the sub-surface rights, or some arrangement between the landowner and his concessionaire. The latter course commonly was followed.[9] The work of the operator involved unavoidable interference with the use of the surface for other purposes, and often the agricultural value of the premises was destroyed for a period far exceeding the productive life of the field. In other ways the interests of the lessor and the lessee might clash, and their relationship afforded numerous occasions for adjustment by legal process. In this early period the nature and the origin of these deposits were shrouded in mystery;[10] the geological conditions favorable to accumulation were unknown;[11] and it was even possible for reasonable and intelligent men to speculate whether the wells might not be tapping reservoirs of natural resources which, like water and air, would be practically inexhaustible.[12] Add to this that the development of the industry coincided with that great post-war period[13] of expansion over the continent and of industrial intensification to which an incisive critic gave the title of "The Great Barbecue,"[14] and it was inevitable that its early his-

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[7]Hail v. Reed, 15 B. Mon. 479 (Ky. 1854).

[8]Cloud, Petroleum Production (1937) *x*.

[9]Shuman, The Petroleum Industry (1940) 45.

[10]1 Summers, Oil and Gas (Perm. ed. 1938) § 3, contains a valuable summary of the theories advanced at various times. And note the language of Judge Snyder in Wood County Pet. Co. v. West Virginia Trans. Co., 28 W. Va. 210, 57 Am. Rep. 659 (1886): "How this gas is formed, whether the supply is limited or inexhaustible, are problems of the future, which observation and experience, as yet, have failed to furnish the means of solving."

[11]Cloud, Petroleum Production (1937) *x*, 47.

[12]See Wood County Pet. Co. v. West Virginia Trans. Co., 28 W. Va. 210, 57 Am. Rep. 659 (1886) wherein Judge Wood said: "Neither the developments of science, nor the evidence in this cause establish, that such gas is likely to be exhausted by its use and consumption. That such may ultimately be the case, is possible, but the fact, if it is such, is not sufficiently certain or apparent to be the basis of a judicial decision."

[13]3 Parrington, Main Currents in American Thought (1930) 7-17.

[14]*Id.* at 23.

tory should be one of riotous economic adventure, characterized by *laissez faire* and a madly acquisitive scramble for nature's bounties.[15]

The legal system which was called to umpire this struggle possessed a traditional technique according to which all those contentions not covered by express statutory enactment were to be decided according to principles resting upon precedent or discovered by deduction from rules illustrated by prior cases, or derived by analogy from decisions in more or less like situations. Since oil and gas in place were part of the physical structure of the earth, the legally recognized rights concerning which had been systematized under the heading of real property, it was natural enough that the courts should turn to this body of law for principles to be applied to these newly important substances. Thus the earlier opinions assumed that the owner of the fee held title to the oil and gas beneath the surface of his tract just as he did to the soil or to the coal, iron or gold that lay thereunder.[16] This resort to the principles of the law of real property furnishes the fundamental basis of the law of oil and gas interests to this day. Thus, in respect to the formalities necessary for the transfer of oil and gas rights, whether by the "lease" for purposes of exploitation[17] or by the alienation of all the landowner's oil and gas rights, compliance with the formalities requisite for the conveyance of realty is essential.[18] For purposes of the Statute of Frauds,[19] of the recording laws,[20] of venue,[21] of the

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[15]SHUMAN, THE PETROLEUM INDUSTRY (1940) 4-7.

[16]Hail v. Reed, 15 B. Mon. 479 (Ky. 1854); Hughes v. United Pipe Lines, 119 N.Y. 423, 23 N.E. 1042 (1890); Northwestern Ohio Nat. Gas. Co. v. Ullery, 68 Ohio St. 259, 67 N.E. 494 (1903); Northwestern Ohio Nat. Gas Co. v. Ullery, 68 Ohio St. 317, 49 N.E. 399, 39 L.R.A. 765 (1897); Stoughton's Appeal, 88 Pa. 198 (1879); Funk v. Haldeman, 53 Pa. 229 (1867); Murray v. Allard, 100 Tenn. 100, 43 S.W. 355, 39 L.R.A. 249 (1897); Williamson v. Jones, 39 W. Va. 231, 19 S.E. 436 (1894).

[17]South Penn. Oil Co. v. Calf Creek Oil & Gas Co., 140 Fed. 507 (N.D. W. Va. 1905). For a useful collection of cases dealing with the formalities necessary in oil and gas leases, see KULP, CASES ON OIL AND GAS (2d ed. 1935) 57-61.

[18]Osborn v. Arkansas Territorial Oil & Gas Co., 103 Ark. 175, 146 S.E. 122 (1912); Right of Way Oil Co. v. Gladys City Oil, Gas & Mfg. Co., 106 Tex. 94, 157 S.E. 737, 51 L.R.A. (N.S.) 268 (1913).

[19]Allen v. Thompson, 169 Ark. 169, 273 S.W. 396 (1925) (royalty interest); Prout v. Hoy Oil Co., 263 Ill. 54, 105 N.E. 26 (1914); Heller v. Dailey, 28 Ind. 555, 63 N.E. 490 (1902) (lease); Sunburst Oil & Gas Co. v. Neville, 76 Mont. 550, 257 Pac. 1016 (1927) (lease); Woodworth v. Franklin, 85 Okla. 27, 204 Pac. 452, 27 A.L.R. 590 (1922) (lease, agent's authority); Montana and Wyo. Oil Co. v. Gibson, 19 Wyo. 1, 113 Pac. 784 (1911) (lease).

[20]Callahan v. Martin, 3 Cal.(2d) 871, 43 P.(2d) 788, 101 A.L.R. 871 (1935) (royalty); Derby Oil Co. v. Bell, 134 Kan. 489, 7 P.(2d) 39 (1931) (lease); Davis v. Lewis, 100 P.(2d) 994 (Okla. 1940) (assignment of oil payment); Tupeker v. Deaner, 46 Okla. 328, 148 Pac. 853 (1915) (lease).

[21]McCully v. McCully, 184 Okla. 264, 86 P.(2d) 786 (1939) (royalty).

homestead laws,[22] of the determination of the privileges of cotenants,[23] and many others,[24] these interests are regarded as interests in realty. The ancient learning relative to land law also has been invoked in the attempt to define the interest of the lessee under an oil and gas lease, although here the judges have been unable to agree upon the results to be deduced.[25]

The traditional plenitude of the powers of the landowner over his domain, the spirit of the time in favor of full individual freedom in all acquisitive activites, and the lack of scientific knowledge pointing to the need for conservation all combined to create in each proprietor the upmost liberty of sinking and exploiting wells. While it became understood fairly early that by wells judiciously located near the boundary line, a man might draw part of the production from beneath his neighbors' premises,[26] it was considered entirely proper so to do. The unfortunate neighbor might neither enjoin the tolling of the oil or gas across the line[27] nor recover damages therefor.[28] His sole recourse was to "go and do likewise."[29] Thus arose the so-called Rule of Capture, stimulating competitive drilling, which is coming to receive such hard words in the literature of recent years.[30]

Still another characteristic of American law in this period was its intense individualism. A heritage of the common law from its puritan background,[31] this characteristic received reinforcement from the spirit of the time,[32] and reached its high-water mark "in the last quarter of the nine-

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[22]Miles v. Jerry, 158 Ark. 314, 250 S.W. 34 (1923); Bruner v. Hicks, 230 Ill. 536, 82 N.E. 888 (1907); Franklin Land Co. v. Wea Gas, Coal & Oil Co., 43 Kan. 518, 23 Pac. 630 (1890); Carter Oil Co. v. Popp, 70 Okla. 232, 174 Pac. 747 (1918).

[23]Callahan v. Martin, 3 Cal.(2d) 871, 43 P.(2d) 788, 101 A.L.R. 871 (1935); Marias River Synd. v. Big West Oil Co., 98 Mont. 254, 38 P.(2d) 599 (1934). See also 2 SUMMERS, OIL AND GAS (Perm. ed. 1938) §§ 222-225, for a discussion of the cases relative to leases executed by co-tenants, life tenants and remaindermen.

[24]Nicholson Corp. v. Ferguson, 114 Okla. 16, 243 Pac. 195 (1926) (statutory measure of damages, title to real property); Sheffield v. Hogg, 124 Tex. 290, 77 S.W. (2d) 1021 (1934) (taxation). But *cf.* First Nat. Bank v. Dunlap, 122 Okla. 288, 254 Pac. 729 (1927) (judgment lien).

[25]For a discussion, see 1 SUMMERS, OIL AND GAS (Perm. ed. 1938) c. 7.

[26]*Cf.* Westmoreland and Cambria Nat. Gas Co. v. De Witt, 130 Pa. 235, 18 Atl. 724, 5 L.R.A. 731 (1889); Brown v. Vandergrift, 80 Pa. 147 (1875).

[27]Kelly v. Ohio Oil Co., 57 Ohio St. 317, 49 N.E. 399, 39 L.R.A. 765 (1897); Hague v. Wheeler, 157 Pa. 324, 27 Atl. 714, 22 L.R.A. 141 (1893). See also Peoples Gas Co. v. Tyner, 131 Ind. 277, 31 N.E. 59, 16 L.R.A. 448 (1892).

[28]Kelly v. Ohio Oil Co., 57 Ohio St. 317, 49 N.E. 399, 39 L.R.A. 765 (1897); Gain v. South Penn. Oil Co., 76 W. Va. 769, 86 S.E. 883 (1915).

[29]Barnard v. Monongahela Nat. Gas Co., 216 Pa. 362, 65 Atl. 801 (1907).

[30]See Hardwicke, *The Rule of Capture and Its Implications as Applied to Oil and Gas* (1935) 13 TEX. L. REV. 391; Oliver, *Oil and Gas Law Responsible for Overproduction and Waste* (1930) 55 A.B.A. REP. 712.

[31]POUND, THE SPIRIT OF THE COMMON LAW (1921) c. II.

[32]See notes 13-15, *supra.*

teenth century."[33] One of its effects upon the law of oil and gas was the leaving of each party to the lessor-lessee relationship to safeguard his own interests. If, in the drafting of the document by which the relationship was created, he failed to make provision for contingencies which might arise, he must bear the loss imposed by his own shortsightedness. Thus a lessor who made no bargain concerning incidental products obtained in connection with the lessee's proper operations was deemed to have abandoned them to the lessee.[34] The lessor who had failed to stipulate upon the subject of development was left to the discretion of the lessee exercised in good faith.[35] If the lease granted an exclusive privilege, the lessor had to respect it.[36] A lessor who had reserved the right to locate wells thereby deprived himself of the right to complain that wells were not drilled where he had specified no location,[37] nor might a landowner who had bargained for the sinking of a certain number of wells contend successfully that the lessee should have been more diligent than the contract called upon him to be.[38] On the other hand, a lessee who had agreed to follow a specific drilling program on pain of forfeiture had to abide the strict letter of his own stipulation,[39] and the unwary speculator who had promised to drill or pay rental for a fixed term discovered to his sorrow that he had to pay for the whole period, although the land had been condemned by neighboring operations.[40]

The emphasis of the strict law upon individual rights found expression also in the rule which conceded to the owner of a well the privilege to use or to waste the product as he saw fit[41] regardless of injury to his neighbor or of depletion of a valuable natural resource.[42] In such instances, "Shall I not do what I will with my own?" was an inquiry as to which the propriety of an affirmative answer was admitted without question.

But there were other factors operative as well. Like every other institution of ours, the law has evolved under the influence of what has been called the "American dream"—that "dream of a land in which life should

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[33]See Pound, The Spirit of the Common Law (1921) 15.

[34]Kier v. Peterson, 41 Pa. 357 (1862); Wood County Pet. Co. v. West Virginia Trans. Co., 28 W. Va. 210, 57 Am. Rep. 659 (1886).

[35]Young v. Forrest Oil Co., 194 Pa. 243, 45 Atl. 121 (1899); Cogan v. Forrest Oil Co., 194 Pa. 234, 45 Atl. 119 (1899); Ammons v. South Penn. Oil Co., 47 W. Va. 610, 35 S.E. 1004 (1900).

[36]Funk v. Haldeman, 53 Pa. 229 (1866).

[37]McKnight v. Manufacturers' Nat. Gas Co., 146 Pa. 185, 23 Atl. 164 (1892).

[38]Stoddard v. Emery, 128 Pa. 436, 18 Atl. 339 (1889).

[39]Brown v. Vandergrift, 80 Pa. 142 (1875).

[40]Edmonds v. Mounsey, 15 Ind. App. 399, 44 N.E. 196 (1899); Wills v. Manufacturers' Nat. Gas Co., 130 Pa. 222, 18 Atl. 721, 5 L.R.A. 603 (1889).

[41]Hague v. Wheeler, 157 Pa. 324, 27 Atl. 714, 22 L.R.A. 141 (1893).

[42]*Cf.* People v. New York Carbonic Acid Gas Co., 196 N. Y. 421, 90 N.E. 441 (1909).

be richer and fuller for every man, with opportunity for each according to his ability or achievement."[43] While that vision in no sense sets as a goal the establishment of a Lubberland, or even a society whose objective is the multiplication of the enjoyment of material goods only, we know that the good life needs must be built upon a sound economic base.[44] The founders of the nation recognized in gross inequalities of property the chief source of social faction and disorder,[45] as did the philosophers from whom they derived their inspiration.[46] Our national instinct has held to this faith since the beginning, and the story of our political struggles might largely be written, without too great exaggeration, in terms of the desire to maintain the opportunity for a broad diffusion of economic prosperity. In the law, likewise, we may find doctrines which stem from the common interest in maintaining the equal economic balance and in promoting the diffusion of material wealth so far as this may be accomplished without undue interference with a system of private property.

The impact of this detail of the ideal picture of the American social order upon the strict individualism with which the law of oil and gas began may be observed in numerous instances. Thus, in view of the inequality in bargaining position between the farmer and the operator with whom the farmer must deal if his land is to be developed and protected, the early insistence upon the delimitation of the legal rights of the parties to the lessor-lessee relationship according to the terms of their agreement alone was modified by the rule that, contrary to the customary interpretation of grants,[47] the oil and gas lease is to be construed most strictly against the lessee. This rule was enunciated as early as 1896,[48] and has been repeated with frequence.[49] Another manifestation of this same viewpoint appears in the judicial insistence upon a public policy that leases should be con-

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[43]See ADAMS, THE EPIC OF AMERICA (1931) 404.

[44]*Id.* at 410, 414.

[45]See the remarks in the Constitutional Convention of 1787 as set forth in DOCUMENTS ILLUSTRATIVE OF THE FORMATION OF THE UNION OF THE AMERICAN STATES (1927) 162, 280, 461 (Madison), 172 (Gerry), 267 (Pinckney), 321, 488 (Governeur Morris). See also Madison's remarks in THE FEDERALIST (1787) No. 10.

[46]See Fellman, *The European Background of Early American Ideas Concerning Property* (1940) 14 TEMP. L. Q. 497.

[47]See 2 TIFFANY, REAL PROPERTY (2d ed. 1920) 1618.

[48]Bettman v. Harness, 42 W. Va. 433, 26 S.E. 271, 36 L.R.A. 566 (1896).

[49]Collections of authorities may be found in 2 SUMMERS, OIL AND GAS (Perm. ed. 1938) § 372; KULP, CASES ON OIL AND GAS (2d ed. 1935) 319 n.; Veasey, *The Law of Oil and Gas* (1920) 18 MICH. L. REV. 652, 661. Summers seems unduly skeptical as to the reality of the rule as an independent criterion of construction, while Veasey's citations suggest a slightly earlier emergence of the rule than the authorities appear to sustain.

strued in favor of development;[50] although here, perhaps, the conviction that the country should be opened up and its natural resources made available as speedily as possible may also play a part in determining the judicial course.[51] A third instance in which it seems apparent that the judicial policy of keeping even the economic balance early moderated the individualism of the strict law is afforded by the duties imposed upon the lessee in favor of the lessor by the doctrine of implied covenants, with which I have dealt at length elsewhere.[52] The strength of the policy lying back of this doctrine is emphasized by the limits which the courts have thrown about the operators' attempts to contract out of the obligations which it entails.[53]

Strict individualism received another blow, in which the advancing knowledge concerning the nature of oil and gas deposits indubitably played a part, when the free right of the landowner and his lessee to operate as they saw fit[54] was limited by the rule that they might not waste the product to their neighbor's injury without benefit to themselves.[55] Furthermore, while entitled to use pumps[56] or other methods to increase the production from the wells on the premises[57] without being limited by the common law doctrine relative to reasonable user of percolating water,[58] they might not

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[50]Paraffine Oil & Gas Co. v. Cruce, 63 Okla. 95, 162 Pac. 716, 14 A.L.R. 952 (1917); Parish Fork Oil Co. v. Bridgewater Gas Co., 51 W. Va. 583, 42 S.E. 655, 59 L.R.A. 566 (1902).

[51]"This construction . . . embodies and enforces that principle of law universally announced by the courts . . . which discourages tying up and rendering unproductive the vast fields of mineral wealth, construes every contract and lease as to both lessor and lessee so as to best promote production, development, and progress, and frowns upon every attempt to evade it as being in contravention of both good morals and public policy." Parish Fork Oil Co. v. Bridgewater Gas Co., 51 W. Va. 583, 42 S.E. 655, 660, 59 L.R.A. 566, 571 (1902). "No unnecessary impediment or delay in the development of the natural resources of the country should be allowed to intervene if the rights of litigants can otherwise be preserved. As far as it is possible, the development should be encouraged to proceed, and not to be abated merely by reason of conflicting claims of litigants." Emde v. Johnson, 214 S. W. 575, 577 (Tex. Civ. App. 1919).

[52]See MERRILL, COVENANTS IMPLIED IN OIL AND GAS LEASES (2d ed. 1940) *passim*.

[53]*Id.* §§ 199-201.

[54]See Hague v. Wheeler, 157 Pa. 324, 27 Atl. 714, 22 L.R.A. 141 (1893), cited *supra* note 41.

[55]Louisville Gas Co. v. Kentucky Heating Co., 117 Ky. 71, 77 S.W. 368, 70 L.R.A. 558 (1903); Higgins Oil & Fuel Co. v. Guaranty Oil Co., 145 La. 233, 82 So. 206, 5 A.L.R. 411 (1919); Gulf Pipe Line Co. v. Pawnee-Tulsa Petroleum Co., 34 Okla. 775, 127 Pac. 252, 41 L.R.A. (N.S.) 1108 (1912).

[56]Higgins Oil & Fuel Co. v. Guaranty Oil Co., 145 La. 233, 82 So. 206, 5 A.L.R. 411 (1919); Jones v. Forest Oil Co., 194 Pa. 379, 44 Atl. 1074, 48 L.R.A. 748 (1900).

[57]People's Gas Co. v. Turner, 131 Ind. 177, 31 N.E. 59, 16 L.R.A. 443 (1892).

[58]For development of the proposition that the inapplicability of this analogy rests upon the special peculiarities of oil and gas as distinguished from other minerals see 1 SUMMERS, OIL AND GAS (Perm. ed. 1938) 128, § 62.

"do any act with reference to the common reservoir . . . injurious to, or calculated to destroy, it."[59]

Acquaintance with the special properties of oil and gas has led to other modifications of the law, particularly in respect to the application of analogies drawn from the law of the land and its more stable mineral constituents. Probably the most striking example is furnished by the extent to which the manifest difficulties presented by the fact that one may lose the oil or gas beneath the surface by drainage to wells on adjoining premises, or by the migration induced by the forces set in motion by the disturbance of nature's equilibrium incident to the development of a field, have brought about the general rejection of the theory of the landowner's absolute ownership of the deposits underneath his land in favor of a doctrine denying such ownership.[60] But other instances may be adduced. Thus, in Pennsylvania a ruling that in the event of the subdivision of land after the execution of a lease, the owners of the respective divisions share in the production from all wells regardless of their location, was justified upon the liability of oil and gas to drainage, as distinguished from the solid minerals which remain in their places.[61] While more mature consideration of the nature of oil and gas rights and of the problems arising from the subdivision of land subject to lease has led most courts to a contrary conclusion,[62] the significant fact remains that the decision to adopt one rule or the other has been founded upon what the judges regarded as the significant facts concerning the nature of oil and gas and the adjustment of property rights therein.[63]

The influence of the experience of the oil business and of developing appreciation of its needs as factors in the evolution of oil and gas law is illustrated in a number of ways. Perhaps the most striking illustration is afforded by the long story of the evolution of the lease form and its adaptation to the changing methods of exploiting our petroliferous natural resources. This story has been so well treated elsewhere[64] that it is as unnecessary as it is impossible, for reasons of length, to detail it here. An-

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[59]Manufacturers' Gas & Oil Co. v. Indiana Gas & Oil Co., 155 Ind. 461, 57 N.E. 912, 50 L.R.A. 768 (1900).

[60]Cases and other authorities are collected in KULP, CASES ON OIL AND GAS (2d ed. 1935) 28 n.

[61]Wetengel v. Gormley, 160 Pa. 559, 28 Atl. 934 (1894).

[62]Cases are collected and discussed at some length in 3 SUMMERS, OIL AND GAS (Perm. ed. 1938) § 608.

[63]For another case in which the peculiar characteristics of oil and gas affected the application of traditional rules of property see Westmoreland & Cambria Nat. Gas Co. v. De Witt, 130 Pa. 241, 18 Atl. 724, 5 L.R.A. 731 (1889).

[64]See Veasey, *The Law of Oil and Gas* (1920) 18 MICH. L. REV. 652, 19 MICH. L. REV. 161.

other illustration is the process of statesmanlike decision whereby a pernicious and unworkable rule which denied the enforcibility against the lessor of leases giving to the lessee an option by means of a "surrender clause" to terminate the relationship[65] was eliminated from the body of the law.[66]

Legislative regulation and the judicial treatment thereof present another phase of the evolution of oil and gas law in which most of the stimulative factors we have discussed have been operating. In the early day, of course, statutory regulation was nil. As time passed, experience in the industry and a widening perception of the nature of the substances with which it dealt combined to produce legislative remedies for a variety of discovered ills. As early as 1878 a Pennsylvania enactment undertook to require the proper plugging of abandoned wells in order to prevent injury to the interests of adjacent landowners and operators.[67] Most of these early statutes were directed toward protecting the underground reservoir from injury through the improper or wasteful operation of the wells which tapped it or through the failure to take adequate precautions to seal off such wells from the producing strata when they ceased to be profitable.[68] They were upheld in the courts, in the face of contentions that they were arbitrary and unreasonable deprivations of liberty and of property without due process of law, on the theory that they protected the interest of all landowners in the preservation of the common source of supply, and in an equitable opportunity to take therefrom, as against rapacious greed or spiteful misuse.[69] To reach such a result, it was necessary that the courts take account of the increasing fund of knowledge concerning the nature of oil and gas and the conditions surrounding their exploitation, the experience of the industry, the relative importance of the interests involved, and the

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[65]Federal Oil Co. v. Western Oil Co., 121 Fed. 674 (C.C.A. 7th, 1902); Berry v. Frisbie, 120 Ky. 837, 86 S.W. 558 (1905); Brown v. Wilson, 58 Okla. 392, 160 Pac. 94, L.R.A. 1917B 1184 (1916); National Oil & Pipe Line Co. v. Teel, 67 S.W. 545 (Tex. Civ. App. 1902); Steelsmith v. Gartlan, 45 W. Va. 27, 29 S.E. 978, 44 L.R.A. 107 (1898).

[66]New American Oil & Mining Co. v. Troyer, 166 Ind. 402, 76 N.E. 253, 77 N.E. 739 (1905); Union Oil & Gas Co. v. Wiedemann, 211 Ky. 361, 277 S.W. 723 (1925); Northwestern Oil & Gas Co. v. Branine, 71 Okla. 107, 175 Pac. 533, 3 A.L.R. 344 (1918); Rich v. Doneghey, 71 Okla. 204, 177 Pac. 86, 3 A.L.R. 352 (1918); Corsicana Petroleum Co. v. Owens, 110 Tex. 568, 222 S.W. 154 (1920); Lovett v. Eastern Oil Co., 68 W. Va. 667, 70 S.E. 707, Ann. Cas. 1912B 360 (1911).

[67]See 1 SUMMERS, OIL AND GAS (Perm. ed. 1938) 292, § 106. Sometimes the statutes have been aimed at the protection of water supplies or of solid mineral deposits such as coal.

[68]*Id.* at 153, 155, § 72.

[69]Ohio Oil Co. v. Indiana, 177 U. S. 190, 20 Sup. Ct. 476, 44 L. ed. 729 (1900); Given v. State, 160 Ind. 552, 66 N.E. 740 (1903); Townsend v. State, 147 Ind. 624, 47 N.E. 19, 37 L.R.A. 294 (1897); Commonwealth v. Trent, 117 Ky. 34, 77 S.W. 390, 4 Ann. Cas. 209 (1903).

ideals of the social order which lie back of the broad standards of decency and reasonableness controlling the substance of governmental regulation which are embodied in the due process clause. The approval given this type of legislation involved a recognition of the need for state interference to protect the private interests of the landowners and operators in a pool against those who sought to subordinate those interests of all to their personal whim or advantage. It did not necessarily recognize a general social interest in the manner of the exploitation of the deposits by the surface owners and their lessees.

The recognition of the social interest in the proper exploitation of oil and gas seems to have come in with the decisions relative to preferred use legislation[70] and to proration.[71] Since these minerals are exhaustible and irreplaceable, the public properly may demand that they not be devoted to relatively unimportant uses, particularly if these may be supplied from other sources. So, too, it does not seem unreasonable to require that in times of overproduction the various wells in a pool shall be subjected to a program of ratable taking in order to eliminate the incentive to waste involved in unrestricted production for a glutted market.

With the recognition of the general interest in controlling the exploitation of oil and gas, advancing technical knowledge has brought new methods of control into play. One by one they have been upheld. It is necessary only to mention regulation of the oil-gas ratio in the production of oil[72] and well spacing.[73] The judicial approval of the latter form of regulation seems to open up the door to compulsory unit operation, should it be desired, at least if the courts can be convinced that difficulties relating to the proper apportionment of the returns to the several tracts involved may be resolved without essential injustice.[74]

This survey, necessarily condensed and imperfect, of the evolution of the law of oil and gas, reveals to us a development in which the progress of science, industrial and business experience, and the demands of the general welfare have united to produce the law as we have it today. There

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[70]Walls v. Midland Carbon Co., 254 U. S. 300, 41 Sup. Ct. 118, 65 L. ed. 276 (1920); State v. Carson Carbon Co., 162 La. 781, 111 So. 162 (1927); Quinton Relief Oil & Gas Co. v. Corp. Comm. of Okla., 101 Okla. 164, 224 Pac. 156 (1924). *Contra:* Gas Products Co. v. Rankin, 63 Mont. 372, 207 Pac. 993, 24 A.L.R. 294 (1922).

[71]Champlin Refining Co. v. Corp. Comm. of Okla., 286 U. S. 210, 52 Sup. Ct. 559, 76 L. ed. 1062 (1932).

[72]Bandini Petroleum Co. v. Superior Court, 284 U. S. 8, 52 Sup. Ct. 103, 76 L. ed. 136 (1931).

[73]Patterson v. Stanolind Oil & Gas Co., 305 U. S. 376, 59 Sup. Ct. 259, 83 L. ed. 231 (1939).

[74]See the discussion in MERRILL, COVENANTS IMPLIED IN OIL AND GAS LEASES (2d ed. 1940) § 227.

has been a constant movement from the extreme individualism of the early law to the emphasis upon the common interest in the proper exploitation and use of these important minerals which appears so generally in the decisions today. At the same time there has been recognition of the place of private property in our legal system and of the consequences which spring therefrom. As new learning has been acquired and as new techniques have been developed, the law has been adjusted to these changes. Rules which obviously hampered proper business practices have been modified or discarded, but the courts have not subordinated the "American dream" to the convenience or the wants of *entrepreneurs*. Within the general pattern thus marked out we may expect the development of this branch of the law to continue.

EXPRESS CLAUSES IN OIL AND GAS LEASES AFFECTING THE USUAL IMPLIED OBLIGATIONS OF THE LESSEE

*A. W. Walker, Jr.**

Since the earliest days of the development of oil and gas law the courts have recognized that oil and gas lessees are under certain implied duties to their lessors unless the leases contained express clauses relieving lessees of these obligations.[1] Disagreements between the lessors and the lessees as to whether these implied duties have been performed have been common. The desire to eliminate the opportunity for such disputes has undoubtedly contributed to the growing use of express clauses in oil and gas leases designed to define the exact nature of the lessee's duties under various specified circumstances. Many clauses restricting the otherwise implied duties of the lessee are attributable to the fact that the majority of oil and gas leases are executed on printed forms prepared or selected by lessees, and it is only natural that they would desire to use a form containing clauses designed to ease the burden imposed by the usual implied covenants. Undoubtedly many lessors execute these leases without full appreciation of the extent to which they are surrendering rights that would otherwise be implied. It is an entirely incorrect picture of the actual situation to assume, however, that all lessors in active oil territory are uninformed or inefficiently represented, and not infrequently lessors insist upon clauses which impose perhaps more onerous burdens upon lessees than the implied duties recognized and enforced by the courts in the absence of contract.

Rarely does the conveyancer have the temerity to attempt to provide expressly and in detail for all possible affirmative duties of the lessee in the development and operation of the leased premises. To endeavor to do so even in the case of a very small tract of land would be exceedingly difficult because of the numerous unknown and unpredictable factors involved, and this difficulty increases proportionately with any increase in the size of the tract of land involved. Usually express clauses merely undertake to affect one or more of the implied covenants

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[1]For excellent treatments of implied covenants, see MERRILL, COVENANTS IMPLIED IN OIL AND GAS LEASES (2d ed. 1940); 2 SUMMERS, OIL AND GAS (Perm. ed. 1938) §§ 391-400.

relating to drilling obligations, to wit: the implied covenant to drill an exploratory well; the implied covenant to develop the premises with reasonable diligence; and the implied covenant to protect the premises against drainage by drilling offset wells.

Different Types of Mineral Conveyances Giving Rise to Implied Covenants

This article will be restricted to a discussion of the use of express clauses affecting the covenants usually implied from the execution of what is commonly called an oil and gas "lease." Similar covenants may be implied in other types of mineral conveyances. For example, the assignor of an oil and gas lease who reserves either an oil payment or an overriding royalty apparently has the benefit of implied covenants similar to those recognized in favor of the lessor.[2] These covenants are frequently affected by express clauses contained in the assignment of the lease.[3] No attempt will be made herein to consider this type of transaction.

It is not always easy to determine whether a mineral conveyance or reservation creates a "lease" relationship between the grantor and grantee. The mere fact that the mineral rights are thereby divided, with the right to receive a royalty upon production vested in one person, and the right to produce vested in another, is not sufficient of itself to establish a "lease" relationship between the two parties. Not infrequently a landowner conveys a royalty interest in the minerals while retaining ownership of the land and of his mineral rights therein. This type of transaction seldom results in the creation of a "lease" between the royalty owner and the landowner, although conceivably it might do so, especially where the entire usual royalty of one-eighth is conveyed.[4]

Where the converse type of situation is presented, that is, where the landowner conveys the mineral rights and reserves a royalty, it sometimes becomes a problem of rather difficult construction to determine whether the parties intended to create a "lease" relationship. This is due primarily to the fact that an oil and gas "lease" is not a fixed form of

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[2]Phillips Petroleum Co. v. Taylor, 116 F.(2d) 994 (C.C.A. 5th, 1941); Note (1938) 16 Tex. L. Rev. 594.

[3]For example see Collins v. Atlantic Oil Producing Co., 74 F.(2d) 122 (C.C.A. 5th, 1934).

[4]In Jackson v. Texas Co., 75 F.(2d) 549 (C.C.A. 10th, 1935), an oil company, owning land in fee simple, conveyed the land but reserved the minerals, it being provided that the grantee should receive a royalty of one-eighth of all minerals produced. In Witt v. Westheimer, 182 Okla. 645, 79 P.(2d) 250 (1938), the grantee of land, as a part of the consideration for the grant, executed a "lease" of the minerals back to the grantor.

instrument. Characteristically, among other clauses, it contains a granting clause, a term clause, royalty clauses, and drilling or delay rental clauses. However, it would seem that only a granting clause and royalty clauses are absolutely essential. Instruments which contain these two clauses, but none of the other clauses mentioned above, present a problem of interpretation in which the court will look at the entire agreement, the consideration paid, the purpose to be accomplished, and all the surrounding circumstances in an effort to determine whether it was the intention of the parties that the grantee should proceed with exploration for, and development of, the minerals. If such was the intention, the instrument will be construed as a "lease," and not as an absolute grant, and the grantee or "lessee" will be bound by the usual implied covenants.[5] On the other hand, if the court concludes that it was the intention of the parties to make an absolute grant of the minerals, no covenant to develop with reasonable diligence will be implied, even though a royalty is retained by the grantor, and even though the instrument contains no express clauses relieving the grantee from the duty to explore and develop the premises.[6] However, it does not necessarily follow that other of the covenants usually implied in oil and gas leases will not be imposed on the grantee, such as the covenant to protect against drainage, or the covenant to exercise reasonable care in conducting all operations. The retained royalty interest alone may be sufficient to support the factual implication of such covenants designed strictly for its protection as distinguished from the implied covenants affecting merely rapidity of accumulation of royalties.[7] Moreover, if such an instrument, although conveying an absolute fee simple in the mineral rights, requires the grantee to do some specific act with regard to the development and operation of the premises, which directly affects the accumulation of royalties, it will

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[5]Crain v. Pure Oil Co., 25 F.(2d) 824 (C.C.A. 8th, 1928); Tennessee Oil, Gas & Mineral Co. v. Brown, 131 Fed. 696 (C.C.A. 6th, 1904); Kentucky Rock-Asphalt Co. v. Miller, 234 Ky. 217, 27 S.W.(2d) 937 (1930); Eastern Kentucky Mineral & Timber Co. v. Swann-Day Lumber Co., 148 Ky. 82, 146 S.W. 438 (1912). See, also, Powell v. Danciger Oil & Refining Co., 134 S.W.(2d) 493 (Tex. Civ. App. 1939, writ of error granted).

[6]Duncan v. Mason, 239 Ky. 570, 39 S.W.(2d) 1006 (1931); Adams v. Elkhorn Coal Corp., 199 Ky. 612, 251 S.W. 654 (1923); Kroeger v. Martin, 72 Okla. 198, 180 Pac. 955 (1919); Loomis v. Gulf Oil Corp., 123 S.W.(2d) 501 (Tex. Civ. App. 1938, writ of error refused); Carpenter v. Smith, 272 S.W. 128 (Tex. Comm. App. 1925); Hynson v. Gulf Production Co., 232 S.W. 873 (Tex. Civ. App. 1921, writ of error refused); Feather v. Baird, 85 W. Va. 267, 102 S.E. 294 (1920).

[7]The writer has found no case specifically passing on this point. *Cf.* Jackson v. Texas Co., 75 F.(2d) 549 (C.C.A. 10th, 1935). It would seem that it could be urged with considerable force that the person having the right to produce should owe some duty to protect the royalty owner against loss from drainage, and that if he should undertake to develop the premises, he should be required to exercise reasonable care.

be implied that the grantee was under the duty to perform this act with reasonable diligence.[8]

Sometimes in instruments wherein the landowner desires to make an absolute grant of the minerals, retaining a royalty interest, the grantee out of an abundance of caution will insist upon the insertion of an express clause negativing the existence of any implied duty to explore or develop. The danger to the grantor of the use of a clause of this kind, unless extreme care is used in its wording, is well illustrated by *Doehring v. Gulf Production Co.*[9] In that case the grantor of the minerals reserved a royalty of one-sixteenth of the net production of oil from the premises, but the instrument expressly provided that the grantee of the minerals was not to be under the duty to drill, develop, or protect against drainage. Thereafter, the grantee executed an oil and gas lease, and the court stated that the effect of this express provision was to prevent such grantor from requiring the lessee of his grantee to develop the premises. The holding is questionable since it would seem obvious that the benefit of this covenant against implied duties was intended to run only with the absolute fee estate conveyed to the grantee, and it should not be held that it would accrue to the benefit of the owner of the lesser leasehold estate carved out of the fee simple estate of the grantee. However, the problem presented could be easily obviated by an express provision in such a conveyance that the clause relieving the grantee from implied duties would not apply to any lessee of the grantee. The court in its opinion also stated that since such grantor was not a party to the lease contract he could not sue for its breach. The royalty owner under these circumstances is a third-party beneficiary of the lease executed by his grantee and should be permitted to sue for the breach of any express or implied covenant contained in the lease.

Express Clauses Relieving a Lessee from Any Duty to Develop or to Protect the Premises

It is very unusual for an oil and gas lease to contain an express clause that the lessee shall be under no implied duties to the lessor unless the instrument contains other express clauses imposing affirmative duties upon the lessee with respect to the development and operation of the premises.[10] Unless the latter is true it is questionable if the term "lease" can be appropriately applied to such an instrument; it partakes more of

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[8]Freeport Sulphur Co. v. American Sulphur Royalty Co., 117 Tex. 439, 6 S.W.(2d) 1039, 60 A.L.R. 890 (1928).

[9]8 S.W.(2d) 723 (Tex. Civ. App. 1928, error dismissed).

[10]See Brooks v. Arkansas-Louisiana Pipe Line Co., 77 F.(2d) 965 (C.C.A. 8th, 1935).

the nature of an absolute or conditional "grant" for the term, if any, stated in the instrument.[11] And in many cases construing such instruments it would seem that the court improperly designated the instrument as a "lease."[12] However, whether the clause appears in a "grant" or in a "lease," the courts will give effect to it as written.[13]

Clauses expressly renouncing the existence of one or more of the usual implied covenants are more common. This is particularly true of the covenant to develop the premises with reasonable diligence. An express clause providing that there shall be no duty to develop will be given effect, although it will be subjected to a strict construction. For example, in *Stanolind Oil & Gas Co. v. Christian*[14] the lease provided that "there shall be no express or implied obligation on the part of lessee *to develop* said premises for oil, gas, or other minerals, either before or after the discovery thereof." It was held that the implied covenant to drill offset wells for protection against drainage was a distinct covenant from the implied covenant to develop, and that the clause in question negatived the existence of the latter, but not of the former, implied covenant.

In other leases the expression is sometimes used that the lessee shall be under no duty "to drill," or that it shall be entirely optional with the lessee as to when he shall "drill."[15] Clauses so worded would seem broad enough to expressly negative the implied covenants to drill an exploratory well, to drill protection wells, and to develop with reasonable diligence. In none of these cases, however, has the court been confronted with the necessity of determining whether the clause would preclude the lessor from any remedy where the land was being drained by wells on adjacent premises. Obviously, the self interest of the lessee would usually cause the drilling of necessary offsets and prevent this problem from arising. However, this is not always necessarily true. If the same lessee was operating the wells on adjacent premises causing the drainage, the incentive to drill an offset might be lacking. The courts have always shown an understandable tendency to protect lessors from destruction of their prop-

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[11]Ralph v. Magnolia Petroleum Co., 95 S.W.(2d) 222 (Tex. Civ. App. 1936, writ of error refused).

[12]Skinner v. Ajax Portland Cement Co., 109 Kan. 72, 197 Pac. 875 (1921); Wilkins v. Nelson, 161 La. 437, 108 So. 875 (1926), and see the unusual instrument involved in Powell v. Danciger Oil and Refining Co., 134 S.W.(2d) 493 (Tex. Civ. App. 1939, writ of error granted).

[13]See the cases cited in notes 10, 11, and 12 *supra*.

[14]83 S.W.(2d) 408 (Tex. Civ. App. 1935, writ of error refused).

[15]Skinner v. Ajax Portland Cement Co., 109 Kan. 72, 197 Pac. 875 (1921); Linn v. Wehrle, 35 Ohio App. 107, 172 N.E. 288 (1928); Ralph v. Magnolia Petroleum Co., 95 S.W.(2d) 222 (Tex. Civ. App. 1936, writ of error refused).

erty rights by drainage, especially where the lessee is responsible for such drainage. It would not be surprising if the courts should interpret clauses of this type as intended by the parties to apply to drilling needed for the development of the premises as distinguished from drilling necessary for its protection, or to find some equitable basis for protecting the lessor.[16]

Rarely will a lessor be so foolish as to execute a lease expressly relieving the lessee from any duty to drill protection wells. Only one instance of a lease of this type has been found in the reported cases.[17] There would seem to be no question as to the validity of the clause if inserted without mistake or fraud.

Another type of clause expressly relieves the lessee from any obligation to "drill" except under certain conditions. Thus, in *Wilkins v. Nelson,*[18] the instrument provided that there was no obligation to drill unless oil "is found in paying quantities within one-half mile of the property." The court upheld the validity of this clause, but left open the question of whether the lease would be subject to annulment if the lessee should defeat any obligation to develop by acquiring the mineral rights on all lands within one-half mile of the premises. This case well illustrates the danger from the lessor's standpoint of making the condition precedent to the obligation to drill one that may be or become subject to the control of the lessee, and this is always a possibility where the condition is the drilling of a productive well within a certain distance from the leased premises.

A somewhat similar clause was involved in *Flewellen v. Simms Oil Co.,*[19] although the problem presented was different. The clause provided that "in no event shall the lessee and his assigns be required to exercise his option to develop said premises in less time than twenty years unless a producing oil or gas well is brought in on an adjoining or adjacent tract of land and that in that event the said lessee shall commence drilling an offset well within six mouths after such well on the adjoining tract has been brought in or else shall forfeit this lease as a penalty for such non-development." It was held that this covenant related only to the drilling of offset wells and that, while it precluded any implied covenant to develop before the necessity for such an offset arose, after production was secured in the offset well the lessee was under the

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[16]Compare the reasoning in Texas Company v. Ramsower, 7 S.W.(2d) 872 (Tex. Comm. App. 1928).
[17]Linn v. Wehrle, 35 Ohio App. 107, 172 N.E. 288 (1928).
[18]161 La. 437, 108 So. 875 (1926).
[19]134 S.W.(2d) 687 (Tex. Civ. App. 1939, writ of error granted).

implied duty to proceed thereafter to develop the premises with reasonable diligence.[20]

Express Clauses Relieving the Lessee From the Implied Duty to Drill an Exploratory Well

Any of the clauses already mentioned which relieve the lessee from the duty to drill or to develop will also negative the existence of any implied duty to drill an exploratory well. However, there are other clauses frequently found in oil and gas leases that are directed specifically at the elimination only of the implied duty to drill an initial or exploratory well, and these clauses require separate consideration.

It is well settled that if an oil and gas lease contains no express provision otherwise the lessee is under the implied duty to commence an exploratory well within a reasonable time after the lease is executed.[21] The mere fact that the lease contains an habendum clause reciting that the lease shall last for a certain number of years and so long thereafter as oil or gas is produced does not preclude the implication of this covenant, and the lessee is not by reason thereof privileged to defer drilling until the end of the fixed term.[22]

This implied covenant seldom arises under modern leases since almost invariably they either contain an express agreement to commence an initial well by a certain date, or provide that the drilling of an initial well may be deferred throughout the fixed term of the lease by the payment of delay rentals. The latter type of clause in the great majority of jurisdictions is held to give the lessee the right, in the absence of drainage, to defer drilling by payment of delay rental for the entire fixed term.[23] In one or two states,[24] however, it has been held that after the lapse of a reasonable length of time the lessor may refuse to accept further delay rentals and demand that the lessee commence a well within a reasonable length of time thereafter upon penalty of forfeiture of the lease for failure to comply with this demand. These jurisdictions have applied the same rule in this regard to fixed-term leases that was generally applied by the courts to no-term leases when

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[20]See also Powell v. Danciger Oil and Refining Co., 134 S.W.(2d) 493 (Tex. Civ. App. 1939, writ of error granted).

[21]Merrill, Covenants Implied in Oil and Gas Leases (2d ed. 1940) 52-60, §§ 15-17.

[22]Mills v. Hartz, 77 Kan. 218, 94 Pac. 142 (1908); Hitt v. Henderson, 112 Okla. 194, 240 Pac. 745 (1925).

[23]Merrill, Covenants Implied in Oil and Gas Leases (2d ed. 1940) 81-87, §§ 27-28.

[24]*Id.* at 87-112, §§ 29-36.

they were in vogue. The position of the minority seems unsupportable since the court, in effect, is substituting a court-made provision for an express contract provision agreed upon by the parties.

No difficulty is presented when the lease specifies a certain date for the commencement of a well. In the absence of drainage, such a clause would preclude any implied duty by the lessee to commence a well at an earlier date. Clauses of this type vary considerably in content. Some impose a duty on the lessee to drill by a certain date; others provide merely that the lease will terminate if a well is not commenced within a specified time; while others merely state that the lessee shall be under no obligation to drill a well before a certain time has elapsed. The courts have given effect to all clauses of this type so long as it clearly appears that the lessee by contract secured the privilege to defer drilling an initial well for a certain period of time. For example, in *McKee v. Thornton*[25] the lease provided that "the lessee or his assigns is to prospect for oil, gas or other minerals or metals within twenty years from the date of this agreement, otherwise this agreement is to be null and void." The court held that this clause negatived any duty on the part of the lessee to drill an initial well before the end of the twenty-year period stated in the lease. Other cases have sustained the validity of similar clauses,[26] and no case has been found in which the courts have refused to enforce a clause of this type because of the length of time allowed the lessee within which to drill an exploratory well.

A very similar type of lease is the modern "fully-paid-up lease." This type of lease, instead of providing for periodic delay rental payments during the fixed term of the lease, contemplates that the initial payment, or bonus, includes compensation for the privilege of deferring drilling during the entire fixed term. Many of these leases contain an express clause that there shall be no obligation to develop during the primary term of the lease. If the lease reveals this intention clearly it would seem that no obligation to drill an initial well, in the absence of drainage, would arise even though the fixed term is for ten years, as is usually true in this type of lease.[27]

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[25]79 Okla. 138, 192 Pac. 212 (1920).

[26]Grooms v. Minton, 158 Ark. 448, 250 S.W. 543 (1923); Ringle v. Quigg, 74 Kan. 581, 87 Pac. 724 (1906).

[27]See Campbell v. Schrock, 50 S.W.(2d) 788 (Tex. Comm. App. 1932). *Cf.* Chapman v. Ellis, 254 S.W. 615 (Tex. Civ. App. 1923, error dismissed).

Express Clauses Affecting the Implied Covenant to Develop with Reasonable Diligence

Clauses entirely relieving the lessee from any duty to develop with reasonable diligence have already been considered. A more common type of provision is one imposing express duties of development upon the lessee intended as a complete or partial substitute for the usual implied covenant to develop with reasonable diligence.

Perhaps the simplest form taken by a clause of this type is one merely changing the standard to be used in gauging compliance with the duty to develop. In most jurisdictions the diligence that must be exercised in developing the premises is that of a prudent operator, although some jurisdictions still adhere to the test of the good faith of the individual operator.[28] In *Magnolia Petroleum Co. v. Page*[29] the lease provided that "the judgment of the lessee, when not fraudulently exercised, in carrying out the purposes of this lease shall be conclusive." It was held that this clause prevented application of the standard of a prudent operation, and that the lessor must establish that the lessee's failure to develop the premises was "fraudulent." Similarly, a clause providing that all development other than the drilling of offset wells should be "at the discretion of lessee" was held effective, the court stating, however, that this did not mean that development should be at the uncontrolled will of the lessee, but that his discretion must be exercised in good faith.[30]

Occasionally leases on land in proven productive territory contain clauses specifying the number of wells to be drilled by the lessee. The greatest caution should be exercised in drafting a clause of this type since it may work injustice to either of the parties. The parties may contract with reference to the development of only one producing horizon, and it may later be determined that several different producing formations underlie the land, and the number of wells specified may be wholly inadequate for proper development. The lessor also runs the risk that drilling will be so intensive on adjacent land as to render his land subject to undue drainage if a larger number of wells than that specified are not drilled. On the other hand, after operations have commenced it may be discovered that the production is not so prolific as the parties had contemplated, and that the number of wells required to

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[28] 2 Summers, Oil and Gas (Perm. ed. 1938) § 416.
[29] 141 S.W.(2d) 691 (Tex. Civ. App. 1940, error refused).
[30] Cowden v. Broderick & Calvert, 131 Tex. 434, 114 S.W.(2d) 1166, 117 A.L.R. 61 (1938).

be drilled is excessive. Obvious complications will also arise if the lessee assigns the lease as to a part of the premises, and such complications are apt to breed litigation and imperil titles. Even where the assignor and assignee agree in the assignment as to the share of the total number of wells each is to drill, it may be that one of them will default in his obligation and thereby endanger the lease of the other. In view of the many objections to this type of clause, it should be used only under exceptional circumstances, and then only with the utmost care in phraseology.

The decisions are uniform in holding that the parties are bound by the express covenant of the lessee to drill a certain number of wells and that no implied covenant to develop exists which would require the drilling of additional wells.[31] Nor, as pointed out in the leading case of *Gulf Production Co. v. Kishi,*[32] will the fact that the number of wells specified are required to be drilled within a certain time justify the inference that the clause was intended only to fix the quantum of diligence during that time and to leave drilling thereafter to be controlled by the implied covenant to develop. The question of whether additional wells can be required if needed to protect against drainage presents an independent problem that will be discussed hereinafter.

Ordinarily a lease simply providing that a well shall be commenced by a certain date, although containing no express provisions for the drilling of additional wells or payment of delay rentals, would probably be construed as not intended to limit the number of wells required to be drilled by the lessee,[33] although there have been leases so worded that the courts have considered the provision for a single well as inconsistent with any implied duty to drill additional wells.[34] The latter cases would suggest the desirability of the inclusion of a clause in such a lease specifically stating that the lessee shall proceed with diligence to develop the premises if oil or gas is discovered, if this is the actual intention of the parties.

Another type of clause having for its purpose the limitation of the number of wells required to be drilled in the development of the premises is one stipulating that the lessee shall never be obligated to drill more

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[31]Hartman Ranch Co. v. Associated Oil Co., 10 Cal.(2d) 232, 73 P.(2d) 1163 (1937); Becker v. Submarine Oil Co., 55 Cal. App. 698, 204 Pac. 245 (1922); Stoddard v. Emery, 128 Pa. 436, 18 Atl. 339 (1889).

[32]129 Tex. 487, 103 S.W.(2d) 965 (1937).

[33]Harris v. Ohio Oil Co., 57 Ohio St. 118, 48 N.E. 502 (1897).

[34]Hughes v. Busseyville Oil & Gas Co., 180 Ky. 545, 203 S.W. 515 (1918); Smith v. Tullos, 195 La. 400, 196 So. 912 (1940).

than one well to a certain number of acres. This clause avoids some, although not all, of the objections noted to a clause fixing the exact number of wells to be drilled. For the lessor's protection it would seem especially desirable to change this clause so that the maximum well density specified would apply to each separate producing horizon underlying the leased premises.

Other types of clauses that may be used for the purpose of affecting and altering the usual implied covenant to develop with reasonable diligence are too numerous for detailed discussion. One of the more common varieties is a clause requiring the lessee, after oil or gas has been discovered, to proceed with development by commencing a new well within a certain number of days after the completion of each prior well.[35] Sometimes the lease permits the lessee to cease further drilling after the completion of the first well, or any subsequent well, and to surrender the lease except as to a certain number of acres around each producing well.[36] And, in the case of gas property, especially where the royalty stated in the lease is a certain annual sum, the option may be given to the lessee of either drilling another well or wells, or of paying the annual gas royalty for such undrilled wells.[37]

Express Clauses Affecting the Implied Obligation to Protect Against Drainage by the Drilling of Offset Wells

The implied covenant to protect the premises against drainage by the drilling of offset wells is more jealously guarded by the courts than is any of the other implied covenants. It requires a clear and unequivocal clause in a lease to convince the courts that the lessor intended to sacrifice the protection given him by this covenant. Indeed, in some jurisdictions the protection given by this implied covenant has been enacted into statute.[38]

A striking example of this attitude of the courts is afforded by the judicial construction that has been given to delay rental clauses in leases when drainage is in progress. In *Texas Co. v. Ramsower*[39] it was held that the acceptance of a rental payment, which under the terms of the lease covered the privilege of deferring the commencement of a

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[35]See the lease involved in Terrell v. Munger Farms Co., 129 S.W.(2d) 407 (Tex. Civ. App. 1939, error dismissed, correct judgment).

[36]Texas Co. v. Wieczorek, 36 Cal. App.(2d) 560, 98 P.(2d) 547 (1940).

[37]Central States Production Corp. v. Jordan, 184 Okla. 262, 86 P.(2d) 790 (1939); Kinder v. Southeastern Gas Co., 115 W. Va. 512, 177 S.E. 193 (1934).

[38]2 Summers, Oil and Gas (Perm. ed. 1938) 346-347, § 399.

[39]7 S.W.(2d) 872 (Tex. Comm. App. 1928).

well for one year, even though acceptance was made after drainage had commenced to the knowledge of the lessor, did not preclude the lessor from recovering damages for the failure to drill an offset well during the year for which the rental had been accepted. It was in effect held that the delay rental clause had no application to the implied covenant to protect against drainage. Many other courts have not gone this far, but it is believed that all courts have gone to the extent of holding that the lessor during the fixed term may refuse to accept a delay rental payment, if drainage is in progress, and demand that the lessee drill a protection well.[40]

Another illustration of this attitude of strict construction against any clause depriving the lessor of protection against drainage is afforded by the case of *Hartman Ranch Co. v. Associated Oil Co.*[41] The lease involved required the lessee to drill only ten wells, but he had actually drilled twelve wells. On adjoining property comparable in size the same lessee had drilled twenty-three wells. In an action to recover damages for failure to protect against drainage the court stated that it was unnecessary to decide whether an express covenant to drill a certain number of wells would exclude an implied covenant generally to drill additional wells to protect against drainage, but that, in any event, the court would not permit a lessee to drain the leased premises by other wells operated by him on adjoining property.

Many leases contain express clauses providing in substance that, if a well producing oil or gas of a certain amount is drilled on adjacent premises and within a certain number of feet of any line of the leased premises, the lessee will drill an offset well. Care should be exercised by the lessor in seeing that the latter distance is sufficient to insure proper protection of the premises. Indeed, it is dangerous for the lessor to agree to any specified distance, for it may be that well-spacing regulations will be adopted preventing the drilling of a well within the distance specified in this clause. Unquestionably the lessor would generally obtain better protection if he relied solely upon the usual implied covenant, or an express covenant couched in the language of the implied covenant. The greatest risk that the lessee incurs in this type of clause is with reference to the stipulated size of well necessitating an offset. A well of a certain size at a shallow depth might be a profitable well, but a well of the same productive capacity at a much deeper depth might be unprofitable.

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[40]Merrill, Covenants Implied In Oil and Gas Leases (2d ed. 1940) § 106.

[41]10 Cal.(2d) 232, 73 P.(2d) 1163 (1937). See also J. M. Guffey Petroleum Co. v. Jeff Chaison Townsite Co., 48 Tex. Civ. App. 555, 107 S.W. 609 (1907). *Cf.* O'Neil v. Sun Co., 123 S.W. 172 (Tex. Civ. App. 1909, writ of error refused).

Even in construing clauses of this type the courts have found opportunity to apply a rule of strict construction so as to extend proper protection to a lessor against drainage.[42] If the clause does not expressly state that it is to be operative both before and after the discovery of oil or gas, the courts have construed it as simply requiring the drilling of an *initial* well on the premises under the circumstances stated in the clause; and, thereafter, the usual implied covenant to protect against drainage is applied by the courts.[43] Lessees careful to obtain the full benefit of this restrictive covenant have avoided these decisions by inserting the express provision that the clause is to apply both before and after the discovery of oil or gas on the premises. Even where the latter type of clause is used it would seem that the implied obligation to develop with the diligence of a reasonably prudent operator would apply after production had been secured, and that the lessee might be required to drill wells in performance of that covenant which could not be required under the restrictions imposed in the offset-well clause, even though performance of that implied covenant might require that the wells be drilled near the property lines of the lease. Unquestionably the mere fact that an oil and gas lease contains an express clause providing for the circumstances under which offset wells are to be drilled, and contains no reference to any other drilling operations, does not preclude the implication of the usual covenant to develop with reasonable diligence.[44]

Where the well on adjacent premises is a gas well, lessees have frequently found it undesirable to drill an offset well because of a want of a market for additional gas in that area. Consequently some leases contain a clause permitting the lessee to pay the lessor a royalty based on the production of the draining well or, if the lease provides for the payment of a certain annual royalty per gas well, of the latter amount, in lieu of drilling an offset well.[45]

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[42]For example, see Geary v. Adams Oil & Gas Co., 31 F. Supp. 830 (E.D. Ill. 1940). However, in Wolter v. Houston Oil Co., 74 S.W.(2d) 706 (Tex. Civ. App. 1934), the court held that an express clause to drill offset wells to wells on "adjoining" premises would not apply to a well on adjacent land separated from the leased premises by another tract of land. The court seemed to leave open the question of whether an implied covenant might not have been relied upon by the lessor.

[43]Magnolia Petroleum Co. v. Page, 141 S.W.(2d) 691 (Tex. Civ. App. 1940, writ of error refused); Humble Oil & Refining Co. v. Strauss, 243 S.W. 548 (Tex. Civ. App. 1922).

[44]Powell v. Danciger Oil & Refining Co., 134 S.W.(2d) 493 (Tex. Civ. App. 1939, writ of error granted).

[45]See the lease involved in Central States Production Corp. v. Jordan, 184 Okla. 262, 86 P.(2d) 790 (1939).

Express Clauses Affecting the Remedies of the Lessor for the Breach of Implied Covenants

Leases frequently contain express clauses modifying or altering the common law remedies available to the lessor for the breach of implied covenants. These may assume an endless variety of forms. Some leases provide that the only remedy for breach shall be an action for damages, and that no action for forfeiture can be maintained; others stipulate that no action for damages can be maintained, but only a suit for cancellation, and provide that the lessee, in any event, shall be entitled to retain a certain number of acres around each drilling or producing well, or well upon which re-working operations are in progress. One of the fairest types of clauses frequently used provides that the lessor must give the lessee written notice of any breach of an implied covenant and a certain number of days thereafter within which to rectify the breach before any action can be maintained.[46] An extreme clause of similar type, but of doubtful validity, is one providing that the lessee shall have a certain number of days after final judicial determination that a breach has occurred within which to comply with the covenant.[47] Any detailed consideration of these clauses would require a discussion of the various remedies afforded by the courts for the breach of each of the implied covenants in oil and gas leases, and would unduly extend the scope of this article.

Conclusion

One fact stands out in any general survey of cases dealing with express covenants affecting the usual implied covenants in oil and gas leases, and that is that the great majority of express clauses have been inserted by lessees in order to restrict or reduce the nature of the obligations imposed by implied covenants. This fact has caused one able writer on the subject to venture the suggestion that if lessees adopt a general practice of inserting express restrictive covenants in fine type in printed form leases the courts may ultimately adopt a policy of refusing to enforce them except where it appears that they were called to the attention of the lessor, and that he freely assented to them.[48] An analogy is suggested to cases dealing with limitations of a carrier's liability printed in fine type on tickets and baggage checks. The analogy between an

[46]See Deace v. Stribling, 142 S.W.(2d) 564 (Tex. Civ. App. 1940); General Crude Oil Co. v. Harris, 101 S.W.(2d) 1098 (Tex. Civ. App. 1937, writ of error dismissed).

[47]See Frick-Reid Supply Co. v. Meers, 52 S.W.(2d) 115 (Tex. Civ. App. 1932). Notice the comment on this case in Merrill, Covenants Implied In Oil and Gas Leases (2d ed. 1940) 432-433, § 201.

[48]Merrill, Covenants Implied In Oil and Gas Leases (2d ed. 1940) 435-438, § 202.

unexecuted and informal instrument, such as a railroad ticket or baggage check, and a formally executed conveyance like an oil and gas lease, seems somewhat strained.

The cases on the whole are uniform in holding that no covenant will be implied where it would be inconsistent with some express covenant in the lease.[49] However, the courts have been inclined to adopt a rather strict construction of any express covenant that tends to diminish, as distinguished from increasing, the duties imposed by the usual implied covenants, and this strict attitude has been particularly noticeable with respect to any express covenant limiting the lessor's right to protection against drainage.

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[49]Brimmer v. Union Oil Co., 81 F.(2d) 437 (C.C.A. 10th, 1936); Brooks v. Arkansas-Louisiana Pipe Line Co., 77 F.(2d) 965 (C.C.A. 8th, 1935); Shell Petroleum Corp. v. Shore, 72 F.(2d) 193 (C.C.A. 10th, 1934); Becker v. Submarine Oil Co., 55 Cal. App. 698, 204 Pac. 245 (1922); Skinner v. Ajax Portland Cement Co., 109 Kan. 72, 197 Pac. 875 (1921); Linn v. Wehrle, 35 Ohio App. 107, 172 N.E. 288 (1928); Central States Production Corp. v. Jordan, 184 Okla. 262, 86 P.(2d) 790 (1939); Stoddard v. Emery, 128 Pa. 436, 18 Atl. 339 (1889); Magnolia Petroleum Co. v. Page, 141 S.W.(2d) 691 (Tex. Civ. App. 1940, writ of error refused); Gulf Production Co. v. Kishi, 129 Tex. 487, 103 S.W.(2d) 965 (1937); Ralph v. Magnolia Petroleum Co., 95 S.W.(2d) 222 (Tex. Civ. App. 1936, writ of error refused); Burt v. Deorsam, 227 S.W. 354 (Tex. Civ. App. 1921).

OIL ROYALTIES: A SUGGESTED CRITERION

*Robert J. Blake**

An analytical approach to a sound classification of oil royalties, from the standpoint of legal incidents, requires a criterion by which the rights and duties of parties to several common transactions concerning fractional interests in petroleum production may be measured. The inconsistencies of the decisions appear to justify a consideration of the subject in the light of fundamental property concepts. Upon such a basis, it is submitted, the true royalty interest possesses the legal incidents of rent. Accordingly, the scope of this article, lest the reader have an aversion for the mysteries of jural fiction, includes a discussion of common law rent, a consideration of royalty as rent, an identification of what properly appear to be true oil royalties, and an application of the suggested test to four transactions common to the industry out of which, it is generally agreed, royalty interests arise. Upon principle, the right to share in production should apply with equal dignity to all components of petroleum in the natural state; hence, the term *oil royalties* is used herein in the collective connotation, embracing oil, gas, casinghead gas and other related hydrocarbon substances.

An interest carved out of an estate at common law was susceptible of classification according to real property principles of the time; and while some of the early property categories have lost their significance with the advent of modern social and economic trends, the basic structure of American real property law remains grounded upon feudal concepts. There is, of course, no advantage to be gained in adhering to legal fiction when modern practice dictates a progressive system of jurisprudence. On the other hand, the historical basis should not be overlooked in seeking the answer to a problem for which the present era offers no precedent.

While there was no common law authority for an object of property rights of value which might be drained from beneath a landowner's premises, *damnum absque injuria,* the majority of petroleum jurisdictions, after considerable verbiage, judicial and otherwise, appear to have adopted a common sense view concerning the nature of oil and gas in its natural state; and it now seems to be generally recognized that whether it is

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regarded that the landowner or his lessee "owns" or has but the "exclusive right" to reduce petroleum to possession, neither view disturbs an application of well settled real property principles.[1] In this connection it is to be observed that common law principles played an important part in discrediting the early analogies of petroleum to solid minerals, subterranean waters, and animals *ferae naturae*.[2] In contrast to the attention given the nature of oil and gas, legal inquiry respecting the essential character of oil royalties has for the most part been but summary. This tendency, together with the complexity of royalty conveyancing practices, usually regarded in law as indigenous to a modern industry, has contributed to a noticeable lack of harmony among the cases both in matters of theory and identification.[3] There is no sound reason, in the writer's opinion, why the oil royalty interest, irrespective of the form it may take, cannot be linked to fundamental principles of the law of real property to the end that an acceptable classification of oil royalties might be established. The purpose of the ensuing discussion of *rent* and its place in the common law is to lay some foundation for the suggestion that present day royalty transactions are not, in the legal sense at least, novel; but are in reality counterparts of conveyancing methods well known to the common law.

Rent

The origin of rent, according to an early authority, was the feudal system of land tenure, wherein the king parcelled out property "in large districts to the great men that had deserved well of him in the

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[1]Adsit, *Oil Estates* (1935) 9 So. Calif. Rev. 299; Haglund, *Evolution and Construction of Oil and Gas Leases* (1928) 3 Temp. L. Q. 239; Kline, *Subsurface Trespassing* (1939) 5 John Marsh. L. Q. 30; Lessar, *Conveyances of Oil Royalties and Mineral Fee Interests in Kansas* (1939) 8 Kan. Bar J. 241; Summers, *The Modern Theory and Practical Application of Statutes for Conservation of Oil and Gas* (1938) 13 Tulane L. Rev. 1; Walker, *Property Rights in Oil and Gas and Their Effect Upon Police Regulations of Production* (1937) 16 Tex. L. Rev. 370; Note (1931) 20 Calif. L. Rev. 220.

[2]A most thorough treatment of oil and gas law as related to fundamental property principles appears in Mills and Willingham, The Law of Oil and Gas (1926) and in Walker, *The Nature of the Property Interests Created by an Oil and Gas Lease in Texas* (1928) 7 Tex. L. Rev. 1, (1929) 8 Tex. L. Rev. 483, (1931) 10 Tex. L. Rev. 291, (1932) 11 Tex. L. Rev. 399. See also Callahan v. Martin, 3 Cal.(2d) 110, 43 P.(2d) 788, 101 A. L. R. 871 (1935).

[3]Oil royalties have been variously treated as rent, as part of the purchase price, and as part of the corpus of the property held by the lessor as an exception from the conveyance. Mills and Willingham, The Law of Oil and Gas (1926) 173. There has been some suggestion that they partake of the incidents of *profits a prendre*. Payne v. Callahan, 37 Cal. App.(2d) 503, 99 P.(2d) 1050 (1940). Both the courts and the researchers have used the following terms in designating a royalty interest: lessor's royalty, overriding royalty, landowner's royalty, participating royalty, non-participating royalty, advance royalty, minimum royalty, percent, bonus, and delay rental.

wars, and were able to advise him in time of peace." Such favorites of the Crown, being unable to use the land to its best advantage themselves, committed parts of it to inferior tenants who were obliged to compensate their overlords for occupation and use of the land by furnishing service or provisions.[4]

The early classification of rents was based primarily upon two things: a right of reversion and a right of distress. Rent reserved by one retaining a reversionary interest in land was identified as *rent service*; and as an incident of tenure, the right of distress belonged to the holder of a reversionary estate *of common right*. The right of distress might be expressed where such common right did not exist, and rent reserved or granted to one without a reversion in the land but with the express right of distress was designated *rent charge*. The remedy of distress was the sole distinction between *rent charge* and *rent sec*; and, inasmuch as this remedy was extended to rents sec by statute in 1730,[5] thereby practically extinguishing this form of rent, only rent service and rent charge need be considered for purposes of the present discussion.[6]

From the above principles, it is to be observed that rent service could properly be created only as an incident to a reversion. It was well settled, after the Statute *Quia Emptores*,[7] that a mere possibility of reverter was of insufficient dignity as a future interest to sustain the reservation of rent service. Rent charge, on the other hand, was not subject to the stringent concept of tenure, and might be created either by reservation upon a conveyance in fee or by grant.

While the background of rent, as it is known today, is generally thought of in terms of rent service, or the ordinary rent reserved upon the conveyance of a leasehold estate, it is of interest to take note of some of the early economic aspects of rent charge. An American writer has observed the following order of society as the reason for prominence of rent charge at common law:

> "All of the wealth of the upper classes, including the church and its monasteries and foundations, consisted in land, and the incomes derived from the services rendered by the cultivators of land to the lords of whom they held. At the same time the sale of land, especially in the large bodies held by the lords, was

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[4] Gilbert, Rents (1758) 1. See also 2 Bl. Comm. *57.
[5] 4 Geo. II, c. 28 (1730).
[6] 2 Bl. Comm. *41; Clark, Covenants and Interests Running with Land (1929) 167; Gilbert, Rents (1758) 15.
[7] Statute of Westminister 3, 18 Edw. I, c. 1 (1290).

> not easy or common. There was no 'market' for it in the modern sense of the word; it was subject to the approbation of superiors, and was opposed by the pride of large possessions. A very natural consequence of the two facts would be that some method should be devised of transferring a definite portion of such rents with the security for their prompt and regular payment, that the landlord himself had, and other advantages of his position as owner; while at the same time the possession of the owner was undisturbed."[8]

The decisions show that the holder of a leasehold estate, as well as the landowner, took advantage of the rent method of raising money, either by reserving a rent upon the assignment of his lease or by granting a rent which placed a charge upon his security, the leasehold estate.[9]

Both rent service and rent charge are recognized in the United States, although the former is by far the more prominent and enjoys the generally accepted meaning of the term *rent*. Rent charge has been actually used in but few jurisdictions in this country, but it is generally agreed that its use is entirely permissible in theory.[10] The following definition taken from Tiffany on *Real Property* indicates American recognition of this species of real property:

> "Rent may be defined, in a general way, as a tribute or return of certain amount, which is regarded as issuing out of the land, as part of its actual or possible profits, and is payable by one having an estate in the land, as compensation for his use, possession and enjoyment of the land, or occasionally, as a charge on the land."[11]

Before leaving the fundamental concept of the criterion selected as a test for the purpose of identifying oil royalties, it appears in order to touch briefly upon certain germane real property principles. Of the objects of property rights, Blackstone says there are three: lands, tenements, and hereditaments, the latter term being all inclusive.[12] Such real property objects may be either corporeal, such as land itself, or

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[8]Hammond, *Rent Charge* (1892) 4 THE GREEN BAG 283, 290. See, also, 2 POLLOCK AND MAITLAND, HISTORY OF ENGLISH LAW (2d ed. 1923) 129; 2 WASHBURN, REAL PROPERTY (5th ed. 1887) 287; WILLIAMS, REAL PROPERTY (5th ed. 1879) 329.

[9]Williams v. Hayward, 1 El. & El. 1040, 120 Eng. Rep. 1200 (Q. B. 1859); Baker v. Gostling, 1 Bing N. C. 19, 131 Eng. Rep. 1024 (C. P. 1834); Newcomb v. Harvey, Garth. 161, 90 Eng. Rep. 699 (K. B. 1690); And see 28 HALSBURY'S LAWS OF ENGLAND (2d ed. 1938) 172; WILLIAMS, REAL PROPERTY (5th ed. 1879) 329.

[10]3 TIFFANY, REAL PROPERTY (3rd ed. 1939) 526; CLARK, COVENANT AND INTERESTS RUNNING WITH LAND (1929) 167; Hammond, *Rent Charge* (1892) 4 THE GREEN BAG 283.

[11]3 TIFFANY, REAL PROPERTY (3d ed. 1939) 524.

[12]2 BL. COMM. *17.

incorporeal, such as certain intangible or invisible rights in land. Rent, either in the form of rent service or rent charge, the authorities are agreed, is a species of incorporeal hereditament,[13] and as such is properly an object of property rights in the same manner as land itself is an object of such rights. In the objective sense, therefore, rent is always real property. Another important connotation of the term *property* relates to the duration of estates therein.[14] If the estate is one for years it is considered a personal property estate, a chattel real at common law; if the estate is one of indefinite duration, as for life, in fee qualified, or in fee simple, it is regarded as a real property estate. Thus, rent from the standpoint of duration may be either real or personal property. The term *rent* is used in still a third sense: the actual payment, in money or kind. Such payment is, of course, personal property.[15]

Royalty as Rent

Having considered something of the theory of rent, it now appears in order to make a brief review of precedent for the suggestion that the true royalty interest possesses the legal incidents of rent, and to consider whether this species of property is the proper object, from the standpoint of legal incidents, with which to associate oil royalties.

Historically, the word *royalty* was of little significance to mining law until the early part of the nineteenth century, when, apparently, this term first came into general use as signifying payment to the landowner by a lessee in return for the privilege of working a mine.[16] The term has since been so applied in both English and American mining law, and undoubtedly from those sources found its way into the law of oil and gas. In general, the mining decisions of both countries have regarded royalty as possessing the legal incidents of rent.[17] In this

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[13] *Id.* at 41.

[14] It is unfortunate that there is a general tendency to use the term *real property* without qualification; or perhaps it is more unfortunate that the common law authorities insisted upon the words *real* and *personal* in the development of procedural fiction.

[15] It is obvious from the above discussion that it is quite correct to speak of rent as either real or personal property, or in a particular case as both, thus emphasizing the importance of using the term qualifiedly.

[16] *Ex Parte* Hankey, 1 M. & McA. 247 (Bank. 1829). As to the derivation of the word *royalty*, consult 8 Oxford English Dictionary (1914) 1852.

[17] *English Mining Decisions:* Barrs v. Lea, 33 L. J. Ch. 437 (Ch. Div. 1864); Regina v. Westbrook, 10 Q. B. 178, 116 Eng. Rep. 69 (1847); Daniel v. Gracie, 6 Q. B. 145, 115 Eng. Rep. 56 (1844); *Ex parte* Hankey, 1 M. & McA. 247 (Bank. 1829).

American Mining Decisions: Von Baumach v. Sargent Land Co., 242 U. S. 503, 37 Sup. Ct. 201, 61 L. ed. 460 (1916); Reynolds v. Hanna, 55 Fed. 783 (C. C. Ohio 1893); Higgins v. California Petroleum and Asphalt Co., 109 Cal. 304, 41 Pac. 1087 (1895); Kissick v. Bolton, 134 Iowa 650, 112 N.W. 95 (1907); Saylor

connection, in contemplation of a subsequent classification of royalties herein, it is to be observed that the precedent referred to above relates only to the royalty reserved by the landowner upon leasing his land for mining purposes and may be regarded as comparable to the royalty reserved by the oil and gas lessor.

In the matter of precedent, the English case of *Regina v. Westbrook*[18] presents something of an apposite illustration, for in that case it was contended that "it is altogether wrong in principle to consider royalty as rent," and the form of conveyance that was before the court suggests something of an analogy to the oil and gas lease. *A* leased land to *B* for brick making purposes for a certain number of years "or till the earth shall be dug out." As part of the compensation for the use of the premises the lessee agreed to pay a royalty of 1*s.* 6*d.* for every thousand of bricks moulded in any one year. A portion of the option reads:

> "We come, then, to the bare objection that the royalty is paid, not for the renewing produce of the land, but for several portions of the land itself, mixed up with foreign matter; the expense of this, however, must of course have been cast off before the royalty itself was fixed. That was a sum, which, after all such expenses paid, the occupier could afford to render to the landlord. When the case is thus laid bare, there is no distinction between it and that of the lessee of coal mines, of clay pits, of slate quarries; in all of these the occupation is only valuable by the removal of portions of the soil; and whether the occupation is paid for in money or kind, is fixed beforehand by contract, or measured afterwards by the actual produce, it is equally in substance a rent; it is the compensation which the occupier pays the landlord for that species of occupation which the contract between them allows. This would not admit of argument in an agricultural lease, where the tenant was to pay a certain portion of the produce; that would be admitted to be in all respects a rent service, with every incident to such a rent; and, in *Daniel v. Gracie* we held the same with regard to a marl pit, and brick mine, as the parties termed it, where the render was of so much per cubic yard of the marl dug, and so much per thousand of the bricks made."[19]

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v. Howard, 229 Ky. 826, 18 S.W.(2d) 279 (1929); Williamson v. Williamson, 223 Ky. 589, 4 S.W.(2d) 392 (1928); Logan v. State Gravel Co., 158 La. 105, 103 So. 526 (1925); State *ex rel.* Interstate Iron Co. v. Armson, 166 Minn. 230, 207 N.W. 727 (1926); Minnesota Loan & Trust Co. v. Douglas, 135 Minn. 413, 161 N.W. 158 (1917); State v. Royal Mineral Ass'n, 132 Minn. 232, 156 N.W. 128 (1916); Graham v. Smith, 170 Va. 246, 196 S.E. 600 (1938).

[18]10 Q. B. 178, 116 Eng. Rep. 69 (1847).

[19]*Id.* at 205, 116 Eng. Rep. at 79.

The American authorities appear, in general, to have followed the English view that mining royalties properly possess the legal incidents of rent. The United States Supreme Court has held that under a lease by which the owner or lessor grants to the lessee the privilege of mining and operating the land in consideration of a certain stipulated royalty on the mineral produced, whatever is paid for the occupation and use of the premises, whether it be in money or kind, is equally in substance rent, and under such circumstances royalties reserved are rentals.[20]

Whether royalty and rent are of such like legal incidents that they may be considered analogous as objects of property rights, is a question which has received little more than passing consideration by a majority of writers in the field of oil and gas law. Some are agreed that royalty reserved to the lessor under an oil and gas lease is properly rent;[21] others consider that inasmuch as the lessee's interest in oil and gas is, upon principle, a *profit a prendre,* it is improper to regard the reservation out of an incorporeal thing as rent.[22] Other objections directed to the analogy, in the light of the early concept of rent, are: rent should be an annual or at least a periodic payment definite in point of time; rent relates to the profits or produce of the land and not to substances which cause its permanent diminution; and, the quantum of rent must be certain.

The view that it is improper to regard a reservation out of an incorporeal thing as rent appears to be the most formidable argument against the suggested comparison, for the foremost common law authorities are explicit in their statements that rent may not be reserved out of an incorporeal hereditament. These authorities support the rule with the feudal reason: "because they are such things in their nature as a man can never recur to for a distress."[23] From the modern viewpoint, the objection that it is improper to regard as rent a reservation out of an incorporeal thing appears open to serious question for two reasons:

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[20]Von Baumach v. Sargent Land Co., 242 U. S. 503, 37 Sup. Ct. 201, 61 L. ed. 460 (1916). See also United States v. Noble, 237 U. S. 74, 35 Sup. Ct. 532, 59 L. ed. 844 (1915).

[21]MILLS AND WILLINGHAM, THE LAW OF OIL AND GAS (1926) 177; THORNTON, LAW OF OIL AND GAS (5th ed. 1932) 368; Adsit, *Oil Estates* (1936) 9 So. CALIF. L. REV. 299; Lesar, *Conveyance of Oil Royalties and Mineral Fee Interests in Kansas* (1939) 8 KAN. BAR J. 241; Walker, *The Nature of the Property Interests Created by an Oil and Gas Lease in Texas* (1928) 7 TEX. L. REV. 1, 40; Notes (1937) 25 CALIF. L. REV. 220, (1939) 27 CALIF. L. REV. 200, (1934) 13 TEX. L. REV. 501.

One of the most extensive arguments which has come to the writer's attention for the proposition that the *lessor's royalty* is properly rent, is contained in the dissenting opinion of Judge Poffenbarger in the case of Musgrave v. Musgrave, 86 W. Va. 119, 103 S.E. 302, 16 A. L. R. 564 (1920).

[22]Simonton, *The Nature of the Interest of the Grantee Under an Oil and Gas Lease* (1918) 25 W. VA. L. Q. 295; Note (1917) 31 HARV. L. REV. 882 (1917).

[23]GILBERT, RENTS (1758) 21.

(1) "Rent can, by the common law authorities, be reserved only out of land or things constituting in law a part of the land, to which the landlord may have recourse to distrain, and cannot be reserved out of incorporeal things. Whether the statement that rent must be reserved out of things to which the landlord may have recourse to distrain is to be regarded as a statement of the reason for the rule precluding the reservation of rent out of incorporeal things, or a statement of the result of the rule does not clearly appear. In favor of the former view reference may be made to statements to be found that the king may reserve rent upon a lease of incorporeal things for the reason that, by virtue of his prerogative, he can distrain on all lands of his lessee, and that rent may be reserved on a demise of the vesture or herbage of land for the reason that the lessor may distrain the cattle on the land. If the common law rule precluding the reservation of rent upon a lease of an incorporeal thing is to be regarded as based on the inability to distrain thereon, the question might arise whether the rule remains the same in any jurisdiction in which, as in the case of most states, the right of distress no longer exists. A differentiation originating in the existence or non-existence of a right of distress may well be ignored after the right of distress has been entirely abolished."[24]

(2) The view that rent may not arise out of an incorporeal thing, in its direction toward a criticism of the royalty-rent theory, overlooks the nature of the lessee's estate in the surface of the lands, which, it is suggested, is corporeal in all instances.[25] Even assuming the right of distress as an incident necessary to rent, it appears that the equipment located on the leased land, which must of necessity be in place before the question may arise, would certainly serve as an object of this common law remedy.

The suggestions that rent should be an annual return and that the return should represent the produce of the land rather than a portion of the land itself, have not been considered of sufficient importance to preclude an acceptance by the English authorities of the principle that mining royalties are properly rent.[26] To quote Halsbury's *Laws of England:* "Rent does not necessarily represent the annual produce of the land; a royalty, notwithstanding that it is reserved in respect of substances which are taken from the land so as to cause its permanent

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[24]2 TIFFANY, REAL PROPERTY (2d ed. 1920) 1465.

[25]For the writer's views concerning the surface interest which the lessee holds under an oil and gas lease, see Blake, *The Oil and Gas Lease* (1940) 13 So. CALIF. L. REV. 324.

[26]See authorities cited *supra* note 17.

diminution, is a true rent."[27] In the matter of certainty, it is well settled that it is sufficient if by calculation and upon the happening of certain events rent becomes certain.[28]

In addition to the aforementioned reasons adverse to the royalty-rent concept, there is a line of decisions in the law of oil and gas which consider royalty as a part of the purchase price for a sale of the minerals and therefore not properly rent. Professor Walker aptly points to the error of this line of reasoning:

> "Nor does the fact that royalties have been regarded as a part of the purchase price and thereby corpus preclude the consideration of them as rents, although it is undoubtedly true that, ordinarily, installments of the purchase money are not to be regarded as rents. However, in the case of a conveyance of land in fee simple with the reservation of a rent in fee simple, the rent is the sole consideration for the conveyance and therefore corpus, but it is nevertheless regarded as rent. And there are a number of situations in which royalties behave much more like rent than like ordinary installments of the purchase price. The covenant to pay royalties runs with the leasehold and binds the purchaser thereof as in the case of a covenant to pay rent. A sale of the surface estate carries with it all unaccrued royalties, although unmentioned. Where land previously devoted to mining purposes is conveyed to, or is inherited by, a tenant for life, the royalties are not regarded as corpus but as ordinary profits from the land and belong to the life tenant. And it has never been intimated that the lessor could retain the superior title to the oil and gas in place because all of the purchase money (royalties) has not been paid, nor that the lessor has an implied vendor's lien on the leasehold estate that would enable him to foreclose for the non-payment of accrued royalties."[29]

It has been suggested that other forms of royalty, such as that granted by the landowner, or that granted or reserved by the lessee, may not properly be considered rent "because to be a rent there must exist a leasehold out of which such rent may arise. [and] A lessee's royalty is not rent, because it is not payable by such lessee to his lessor."[30]

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[27] 20 HALSBURY'S LAWS OF ENGLAND (2d ed. 1938) 158.

[28] "The rent must be certain, or that which may be reduced to a certainty. . . . And the rent may as well be delivered in hens, capons, roses, spurs, bows, shafts, etc. or other profit that lieth in render, office, attendance, and such like as in payment of money. In the present instance, however, the rent is reserved in money: and the amount is, according to the criterion of Lord Coke, capable of being ascertained . . . by the number of cubic yards or marl and slack got in the one case, and of bricks in the other." Daniel v. Gracie, 6 Q. B. 145, 115 Eng. Rep. 56 (1844).

[29] Walker, *The Nature of the Property Interests Created by an Oil and Gas Lease in Texas* (1928) 7 TEX. L. REV. 1, 41.

[30] Levy, *Oil Royalties—A Distinct Species of Property* (1938) 11 So. CALIF. L. REV. 319, 324.

In view of the aforementioned well defined aspects of rent charge, such reasoning is, of course, untenable.

Certain outstanding contributions to the law of oil and gas clearly point to the fact that a thorough knowledge of the law of real property is necessary to an understanding of the law of oil and gas.[31] In respect to the lessee's interest, the early "migratory" concept of petroleum deposits, and an attendant development of rules of construction regarded as essential to the law of oil and gas, contributed to a divergence from fundamentals in many of the early cases.[32] Perhaps the revival of the *profit a prendre* (which Washburn at one time considered so long out of existence that it was unworthy of discussion) in its relation to a solution of the problem concerning the lessee's interest under an oil and gas lease, may be paralleled to a degree by mature consideration of rent as the proper jural standard for true oil royalties.[33]

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[31]See MILLS AND WILLINGHAM, THE LAW OF OIL AND GAS (1926); Veasey, *The Law of Oil and Gas* (1919) 18 MICH. L. REV. 445, (1920) 19 MICH. L. REV. 161; Walker, *The Nature of the Property Interests Created by an Oil and Gas Lease in Texas* (1928) 7 TEX. L. REV. 1, (1929) 8 TEX. L. REV. 483, (1931) 10 TEX. L. REV. 291, (1932) 11 TEX. L. REV. 399.

[32]For a discussion of the effect of the early concept of oil and gas in the natural state, see Haglund, *Evolution and Construction of Oil and Gas Leases* (1928) 3 TEMP. L. Q. 239; Veasey, *The Law of Oil and Gas* (1919) 18 MICH. L. REV. 445, 452; Walker, *Fee Simple Ownership of Oil and Gas in Texas* (1927) 6 TEX. L. REV. 125.

The one time prominent "migratory" concept is well illustrated by the following quotation from an early Texas case: "They are supposed to percolate restlessly about under the surface of the earth, even as the birds fly from field to field and the beasts roam from forest to forest." Medina Oil Development Co. v. Murphy, 233 S.W. 333, 335 (Tex. Civ. App. 1921). Geologists and petroleum engineers are now of the universal belief that oil and gas, once confined to a given reservoir, move from beneath a particular landowner's premises only when another taps a common zone of production. See HARDWICKE, INNOCENT PURCHASER OF OIL AND GAS LEASE (1921) 7; 1 SUMMERS, OIL AND GAS (Perm. ed. 1938) c. 1.

[33]The view that the lessee's interest in and to petroleum which may underlie the leased land is properly a *profit a prendre* has found expression in both "exclusive right" and "ownership" jurisdictions, and has received considerable support among writers in the field.

Exclusive right jurisdictions: Francis v. Superior Oil Co., 102 Fed.(2d) 732 (C.C.A. 10th, 1939); Callahan v. Martin, 3 Cal.(2d) 110, 43 P.(2d) 788, 101 A. L. R. 871 (1935); Campbell v. Smith, 180 Ind. 159, 101 N.E. 89 (1913); Heller v. Dailey, 28 Ind. App. 555, 63 N.E. 490 (1902); Rich v. Doneghy, 71 Okla. 204, 177 Pac. 86, 3 A. L. R. 352 (1918). See McIntosh v. Leslie, 13 Ont. L. R. 54 (1907); *cf.* Rives v. Gulf Refining Co. of Louisiana, 133 La. 178, 62 So. 623 (1914).

Ownership Jurisdictions: Burden v. Gypsy Oil Co., 141 Kan. 147, 40 P.(2d) 463 (1935); Brinkman v. Empire Gas & Fuel Co., 120 Kan. 602, 245 Pac. 107 (1926); Willard v. Federal Surety Co., 91 Mont. 465, 8 P.(2d) 633 (1932); Homestake Exploration Corp. v. Schoregge, 81 Mont. 604, 264 Pac. 388 (1928); Funk v. Haldeman, 53 Pa. 229 (1866); Boatman v. Andre, 44 Wyo. 352, 12 P.(2d) 370 (1932).

For a discussion of the *profit a prendre* and its relation to the law of oil and gas, see Adsit, *Oil Estates* (1936) 9 So. CALIF. L. REV. 299; Blake, *The Oil and Gas Lease* (1940) 13 So. CALIF. L. REV. 304, 393; Greer, *Ownership of Oil and Gas in Place* (1921) 1 TEX. L. REV. 162; Lesar, *Conveyance of Oil Royalties and Mineral Fee Interests in Kansas* (1939) 8 KAN. BAR J. 241; Poole, *The Nature of the*

Identification of Oil Royalties

Cursory judicial attention to the subject of oil royalties has brought about two quite apparent consequences. First, it is not uncommon to find among the cases the term *royalty* applied to any payment related to petroleum exploration or production, thus grouping under one heading factual situations which may or may not concern interests in real property. Second, a confusing array of royalty terminology has found its way into the decisions, with little standardization of usage or meaning.[34]

In view of these factors it is, of course, desirable that the subject matter under discussion be clearly identified. Such an identification requires not only that royalties be isolated from other payments related to petroleum operations, but also that the several types of royalty interests be clearly defined. As to the first point, the Supreme Court of Oklahoma has made the following pertinent statement:

> "'The word 'bonus' has a definite meaning in the oil and gas industry. It is defined in Bouvier as a premium paid to a grantor or vendor, and strictly is the cash consideration or down payment paid or agreed to be paid for the execution of an oil and gas lease.
>
> "'The term 'rental,' as used in oil and gas leases, refers to the consideration paid to the lessor for the privilege of delaying drilling operations.[35]

Lessee's Interest Under an Oil and Gas Lease in Kansas (1937) 5 Kan. Bar J. 306; Simonton, *The Nature of the Interest of the Grantee Under an Oil and Gas Lease* (1918) 25 W. Va. L. Q. 295; Veasey, *The Law of Oil and Gas* (1919) 18 Mich. L. Rev. 749. See also 40 C. J. 978, § 564; Hardwicke, Innocent Purchaser of Oil and Gas Lease (1921) 35; Notes (1937) 26 Calif. L. Rev. 359, (1917) 31 Harv. L. Rev. 882, (1939) 46 W. Va. L. Q. 66.

[34]Of the terms mentioned in note 3 *supra* which have been used to designate a royalty interest, those which are not given further treatment herein are:

Advance royalty: a sum paid either for delay during exploration, or as a minimum royalty which is allowable as credit to the lessee against subsequent accruing royalty. *Advance royalty* is not to be confused with *delay rental,* the latter form of payment not being deductible from subsequent accruing royalties. See Prarie Oil Co. v. Schacht, 75 Okla. 101, 181 Pac. 731 (1919); Mills and Willingham, Law of Oil and Gas (1926) 183.

Minimum Royalty: "The term applied when the lease calls for a certain minimum sum of money or amount of production which lessee is bound to pay whether the amount produced would bring the royalty up to that amount or not. The provision is common in the case of solid minerals, but uncommon in commercial oil and gas leases." Mills and Willingham, Law of Oil and Gas (1926) 183. See State v. Cavour Mining Co., 143 Minn. 271, 173 N.W. 415 (1919) for a case which points out the distinction between *minimum* and *advance* royalty.

Percent: This term, together with the term *participating royalty* is generally used to designate a right arising out of a contract to pay out of production.

Non-Participating Royalty: Another term for the interest treated herein as *landowner's royalty.*

[35]This term is perhaps more commonly known as "delay rental." Mills and Willingham, Law of Oil and Gas (1926) 136.

> "The term 'royalty' in the strict sense is held to mean a share of the product or proceeds therefrom, reserved to the owner for permitting another to use the property."[36]

A further step in the separation of true royalties from other forms of payment is the elimination from the royalty classification of rights arising out of contracts to pay out of production. This distinction is based upon the principle that the true royalty interest, partaking of the legal incidents of rent, is an interest in real property.[37]

Occasionally, as a basis for determining the existence of a royalty interest, the test as to whether payment out of production is to be made in money or kind is employed. Such distinction, it is generally agreed, is without merit, for the right to share is of like legal effect, irrespective of the manner of payment agreed upon by the parties.[38] The same distinction was advanced at common law with respect to rent, but the authorities have long stressed the rule that rent might properly be payable either in money or kind.[39]

As to the identification of royalty interests, perhaps the most suitable means of classification is by way of example. While the royalty terms employed in the following grouping are to a degree arbitrary, they suggest themselves as suitable terminology for the purpose of separating with some degree of accuracy distinct types of royalty interests.

1. *Lessor's royalty:* *A* grants to *B*, for a term of years *or* for a term of years and so long thereafter as oil and gas are produced, the exclusive right to enter upon a particular parcel of land and extract oil and gas, *A* reserving one-eighth of all oil and gas produced, extracted and saved.[40] The term *lessor's royalty* merely designates that royalty payable to the lessor under an oil and gas lease.

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[36]Carroll v. Bowen, 180 Okla. 215, 217, 68 P.(2d) 773, 775 (1937). See also Wright v. Bush, 116 F.(2d) 265 (C.C.A. 10th, 1940); Elsinore Oil Co. v. Signal Oil & Gas Co., 3 Cal. App.(2d) 570, 40 P.(2d) 523 (1935); Geller v. Smith, 130 Cal. App. 485, 20 P.(2d) 102 (1933); Davis v. Hurst, 150 Kan. 130, 90 P.(2d) 1100 (1939).

[37]From the purchaser's viewpoint, there is probably little distinction between a contract to pay out of production and an *overriding royalty granted.* (The latter term is discussed herein on page 322 *infra.*) For this reason it has been suggested that a promise to pay out of petroleum production be regarded as an equitable lien or charge on real property. Note (1937) 26 CALIF. L. REV. 480, 486. See also Davis v. Lewis, 100 P.(2d) 994 (Okla. 1940).

[38]In this connection some authorities profess to find a line of cleavage between fractional interests in gross and net production. The fundamental incident of rent, in this respect, is only that rent be definitely ascertainable. Upon principle, "the scale by which the rent is measured, *i. e.*, by gross or net production should not of itself change the nature of the interest." Note (1937) 26 CALIF. L. REV. 480, 481.

[39]See the authorities cited in the discussion of *Rent, supra* p. 308.

[40]While one-eighth appears to be the usual royalty rate, the quantum of royalty reserved to the lessor varies, of course, with conditions in a particular area.

2. *Landowner's royalty:* *A* grants to *C,* his heirs and assigns, 3% of all oil and gas produced, extracted and saved upon a particular parcel of land. The term *landowner's royalty* appears applicable to *C*'s interest in that such royalty is created by grant of the landowner.

3. *Overriding royalty reserved:* *B,* an oil and gas lessee, assigns his leasehold estate to *X, B* reserving 2% of all oil and gas that may be produced, extracted and saved. The term *overriding royalty* is perhaps best known in relation to this form of transaction, implying a royalty payable out of production over and above that payable to the lessor.[41] The word *reserved* is added here in order to distinguish this royalty interest from the fourth classification set out below. *Overriding royalty,* as a means of identification without qualification, is very apt to be misleading inasmuch as it has been used more or less as a catch-all royalty term.[42]

4. *Overriding royalty granted:* *B,* an oil and gas lessee, grants to *Y,* a speculative investor, 2% of all oil and gas that may be produced, extracted and saved under *B*'s lease. The term employed to designate this form of royalty is distinguished from the above type of override merely by the appropriate word of identification relative to the manner of its creation.

Of course, once the above royalty interests have been created, they may be freely transferred; but they should not for this reason necessarily lose their legal identity; nor should the fact that the interest may be created for a greater or less period of time than that referred to in the several illustrations have any bearing upon the particular type of royalty.[43]

Lessor's Royalty

A *grants to* B, *for a term of years or for a term of years and so long thereafter as oil and gas are produced, the exclusive right to enter upon a particular parcel of land and extract oil and gas,* A *reserving one-eighth of all oil and gas produced, extracted and saved.* In general, two concepts govern the decisions which settle for a particular juris-

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[41]Mills and Willingham, Law of Oil and Gas (1926) 184.

[42]Professor Summers suggests that "Perhaps the only safe way to define the term 'overriding royalty' is to say that it is a fractional interest in the gross production of the oil and gas, in addition to the usual royalties paid to the lessor." 3 Summers, Oil and Gas (Perm. ed. 1938) 317, § 554. From the variety of usage given the term, such a definition, while undoubtedly sound, points to the necessity of a qualified use of "overriding royalty."

[43]The reader may wish to consider further the above illustrations in relation to modern royalty forms. For a variety of such forms, see Oakes, Benoits Oil and Gas Forms (2d ed. 1939) 155.

diction the nature of the lessee's interest under an oil and gas lease.[44] One view, and perhaps the better reasoned, is that the lessee's interest in petroleum in the natural state is in the nature of a *profit a prendre;* the other is that the lessee takes a conveyance of the minerals in place. Neither view appears to militate against an acceptance of the royalty-rent theory, for as suggested heretofore, it seems altogether proper to say that a true rent may be reserved out of the lessee's estate whether it be regarded as corporeal or incorporeal.[45] In this connection, there is substantial support for the principle that the lessor's royalty is properly rent in both "exclusive right" and "ownership" jurisdictions.[46]

It does not appear of consequence to an application of the suggested criterion whether the analogy be drawn to rent service or to rent charge. All forms of rent at common law were classed as incorporeal hereditaments, real property in the objective sense, and in theory represented a right to share in profits of the land. If the oil and gas lease is for a term of years, the royalty reserved is analogous to rent service, the landowner retaining a reversionary interest out of the estate granted; if the oil and gas lease is for a term of years and "so long thereafter as oil and gas is produced"—a limitation generally recognized as vesting in the lessee a determinable fee estate either in the *profit a prendre* or in the oil and gas in place (as the case may be)—the royalty reserved is analogous to rent charge, the landowner retaining as to the estate granted but a possibility of reverter.[47]

Landowner's Royalty

A *grants to* C, *his heirs and assigns, 3% of all oil and gas produced, extracted and saved upon a particular parcel of land.* The practice of landowners in granting oil royalties would seem to be a direct descendant

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[44]See authorities cited *supra* note 1.

[45]See discussion under *Royalty as Rent, supra* p. 313.

[46]Arrington v. United Royalty Co., 188 Ark. 270, 65 S.W.(2d) 36, 90 A. L. R. 765 (1933); Callahan v. Martin, 3 Cal.(2d) 110, 43 P.(2d) 788, 101 A. L. R. 871 (1935); Miller v. Carr, 188 So. 103 (Fla. 1939); McIntire's Administrators v. Bond, 227 Ky. 607, 13 S.W(2d) 772, 64 A. L. R. 630 (1929); Robertson v. Pioneer Gas Co., 173 La. 313, 137 So. 46 (1931); Homestake Exploration Corp. v. Schoregge, 81 Mont. 604, 264 Pac. 388 (1923); Sheffield v. Hogg, 124 Tex. 290, 77 S.W.(2d) 1021 (1934); Mills and Willingham, Law of Oil and Gas (1926) 177; Thornton, Law of Oil and Gas (5th ed. 1932) 368; Adsit, *Oil Estates* (1936) 9 So. Calif. L. Rev. 299; Lesar, *Conveyance of Oil Royalties and Mineral Fee Interests in Kansas* (1939) 8 Kan. Bar J. 241; Walker, *the Nature of the Property Interest Created by an Oil and Gas Lease in Texas* (1928) 7 Tex. L. Rev. 1, 40; Notes (1939) 27 Calif. L. Rev. 200, (1937) 25 Calif. L. Rev. 220, (1934) 13 Tex. L. Rev. 501.

[47]For a particularly thorough consideration of the determinable fee estate and its relation to the law of oil and gas, see Walker, *The Nature of the Property Interests Created by an Oil and Gas Lease in Texas* (1938) 7 Tex. L. Rev. 1, 15.

of the common law custom of placing a rent charge upon land as a means of raising money upon a real property security, which, as previously mentioned, is not altogether unknown to modern realty practices.

There would appear to be no practical difficulty in determining the rights of the holder of a landowner's royalty whether such royalty is created where there is or is not an oil and gas lease on the lands at the time such royalty interest is created. As between the royalty holder and the lessee, the maxim *prior tempore potior jure* would, of course, govern. As between the royalty holder and the lessor, while it might be contended that the *landowner's royalty* holder took with notice of the lessor's interest under the lease, the intent of the parties from all of the circumstances surrounding the royalty transaction should, upon principle, control.[48]

Overriding Royalty Reserved

B, *an oil and gas lessee, assigns his leasehold estate to* X, B *reserving 2% of all oil and gas that may be produced, extracted and saved.* It was quite proper, at common law, to reserve a rent upon the assignment of a lease, such rent separated from the reversion being, of course, rent charge.[49] The analogy again appears to be in order, and while the oil and gas authorities have not, manifestly, delved deeply into the subject, there is some authority for the view that royalty reserved upon the assignment of an oil and gas lease is properly rent.[50]

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[48]For a discussion of this type of royalty, see Alexander v. King, 46 F.(2d) 235 (C.C.A. 10th, 1931); Callahan v. Martin, 3 Cal.(2d) 110, 43 P.(2d) 788, 101 A. L. R. 871 (1935); Bellport v. Harrison, 123 Kan. 310, 255 Pac. 52 (1927); Lesar, *Conveyance of Oil Royalties and Mineral Fee Interests in Kansas* (1939) 8 Kan. Bar J. 241. In the case of *Callahan v. Martin, supra,* the court, after pointing out that the *lessor's royalty* is analogous to rent, decided that the landowner's royalty is an interest in the nature of a *profit a prendre.* The instrument before the court in that case entitled the holder thereof to "three percent of all oil and gas and other hydrocarbon substances and/or minerals produced, extracted and saved on the following described property." It is submitted that the court in that case confused the right to share in the proceeds of development—a true royalty or rent—with the right to drill for and produce oil and gas—a *profit a prendre.* For a more detailed discussion of the case, see Blake, *The Oil and Gas Lease* (1940) 13 So. Calif. L. Rev. 393, 416.

[49]Williams v. Hayward, 1 El. & El. 1040, 120 Eng. Rep. 1200 (Q. B. 1859); Baker v. Gostling, 1 Bing N. C. 19, 131 Eng. Rep. 1024 (C. P. 1834); Newcomb v. Harvey, Carth. 161, 90 Eng. Rep. 699 (K. B. 1690). See also McMurphy v. Minot, 4 N. H. 251 (1827); Van Rensselaer v. Hays, 19 N. Y. 68, 75 Am. Dec. 278 (1859); Marshall v. Conrad, 5 Cal. 364 (Va. 1805).

[50]Homestake Exploration Corp. v. Schoragge, 81 Mont. 604, 264 Pac. 388 (1928); Tennant v. Dunn, 110 S.W.(2d) 53 (Tex. Comm. App. 1937); Frost v. Standard Oil Co. of Kansas, 107 S.W.(2d) 1037 (Tex. Civ. App. 1937); Daggett, Louisiana Mineral Rights (1939) 197; Mills and Willingham, The Law of Oil and Gas (1926) 233; Note (1937) 26 Calif. L. Rev. 480, 484.

Overriding Royalty Granted

B, *an oil and gas lessee, grants to* Y, *a speculative investor, 2% of all oil and gas that may be produced, extracted and saved under* B's *lease.* This form of royalty is much the same, from the standpoint of common law conveyancing practices, as the landowner's royalty, except that it is effective as a charge upon the estate of the lessee rather than that of the landowner. In the matter of precedent it is sufficient to say that from time to time the practice of holding property for a long term of years was not uncommon in England, and leaseholds of such duration, being of substantial value, served as ample security for a rent charge upon a leasehold estate. There appears to be no distinction, in theory, between this common law realty practice and the modern device employed by small operators for the purpose of obtaining development funds.[51]

It is to be observed that this brief discussion of the subject of oil royalties is confined, primarily, to royalty in the objective sense, that is, royalty as a species of real property. The acknowledgement that the true royalty possesses the legal incidents of rent offers a basis for critical consideration of not infrequent statements among some decisions that royalty is real property, among others that it is personalty. Such statements, without qualification, are unfortunately a result of hasty judicial review. For the term *royalty* is used in three distinct senses: as an object of property rights, as respecting quantum of the estate therein, and as the actual payment made or to be made to the holder of a royalty interest. Within the meaning of the suggested criterion, royalty, as an object of property rights, is real property. In respect of duration, the royalty holder may enjoy a real property estate, as where the extent of his interest is fee simple or fee qualified, or he may be vested with a personal property estate, as where the extent of his interest is for a term of years.[52] The actual payment of accrued royalty is, of course, personal property. To further emphasize the importance of qualifying the term *royalty,* it may be said that in the objective sense royalty is always real property, that in the duration sense royalty may be either real or personal property, and that in the payment sense royalty is always personal property.

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[51]See Fairburn v. Eaton, 6 Cal. App.(2d) 264, 43 P.(2d) 113 (1935); Frost v. Standard Oil Co. of Kansas, 107 S.W.(2d) 53 (Tex. Comm. App. 1937); 3 Summers, Oil and Gas (Perm. ed. 1938) 332, §556.

[52]Fundamental real property principles discussed in connection with *Rent,* discussed p. 308 *supra,* are of course applicable to *royalty,* assuming an acceptance of the suggested criterion.

ROYALTY IN LOUISIANA*

Harriet S. Daggett†

Terminology

Agreement upon terms should be the first consideration between writer and reader, so that the "tyranny of words" may not prevent an intelligent exchange of ideas. The need for exact words designating royalty rights increases as the rights evolve legally. Louisiana is not free from terminology difficulties any more than are other jurisdictions.[1] Crystal phrases which are free from lengthy explanations and have clear-cut legal connotations that may be counted upon to always mean the same thing are not available. It may be said at this time that two large classifications of royalty may be made, which will be termed *rent royalty* and *royalty per se*. The first category includes overriding royalty.[2] Subdivisions according to the substance involved are oil royalty, gas royalty, and casinghead gas royalty. Other subdivisions will undoubtedly appear as presently known or subsequently discovered substances indicate limiting or designating words. Again, there is difficulty and difference of opinion even as to the names of the *substance!* For example, "the hydrocarbon fraction which liquifies on reduction in pressure in the retrograde range"[3] is now becoming a matter of importance and may or may not give legal trouble. This substance has been termed "distillate," "water white oil," and "condensate." The term "distillate" seems to be the most frequently used, but is objected to by technicians, who properly point out that it is a refining term rather than a production term and that the word "condensate" should be used.[4]

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*This discussion of the Louisiana Law of Royalty is offered in addition to Mr. Robert J. Blake's discussion of that subject (found *supra* page 307) because of the fact that Louisiana is a civilian state whose concepts of royalty differ in material respects from those usually expressed in the common law states.

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[1]Dabney-Johnston Oil Corp. v. Walden, 4 Cal.(2d) 637, 52 P.(2d) 237 (1935), cited by Levy, *Oil Royalties—A Distinct Species of Property* (1938) 11 So. Calif. L. Rev. 319, 320; Daggett, Mineral Rights in Louisiana (1939) 175 *et seq.*, §59; Glassmire, Law of Oil and Gas Leases and Royalties (2d ed. 1938) 67 *et. seq.*, §21.

[2]See Daggett, *op. cit. supra* note 1, at 197, § 62; Blake, *The Oil and Gas Lease—Part II* (1940) 13 So. Calif. L. Rev. 393, 419 and n. 199c.

[3]Weber, *Recycling Trend Expands with Bigger Gas Reserves* [n.d.] Gas Recycling and Distillate Recovery (a survey compiled and reprinted by Clark Bros. Co., Inc.) 1.

[4]*Ibid.*

A generally used term for rent royalty is "lessor's royalty."[5] The terms "lessors," "lessee's," and "sub-lessor's"[6] are helpful in discussing the rights of the various parties to lease contracts. In every case that royalty arises out of or is incidental to a lease contract, it may properly be called "rent," the accepted term designating the consideration for a lease.

When royalty is *not* consideration for a lease and does not arise from nor accompany such a contract, then a different legal concept results and a different term must be used to disassociate the connotations flowing to the mind from the lease idea. Royalty per se as distinguished from rent royalty is spoken of by the Louisiana court as *royalty,* without a modifying word. In some states this type is termed "landowner's" royalty, a none too happy phrase as a bearer of expected connotations, because the owner of this royalty may or may not be the owner of the land. Obviously, all royalty issues originally and by some circuit from a landowner. Furthermore, the landowner's share from a lease might suggest itself. However, the term is probably no more inaccurate than rent royalty or lessor's royalty and apparently has sufficiently fixed connotations to be of reasonable service in the conveying of an idea. But, one writer calls it "royalty properly so-called,"[7] a more satisfactory term in the writer's judgment. The Louisiana court in the case of *Vincent v. Bullock*[8] refused to name the newly born interest. They said:

> "It is immaterial what term is used in characterizing the interest reserved by the plaintiffs, because they have, by clear and unmistakable language, described the interest reserved by them. . . . "[9]

The word "royalty" alone was used in the instrument.

The court also approved in italics the statement that, *"The legal nature of royalty must be grounded upon the contract in which it appears. . . . "*[10] However, the court seems to refer to this type, new in Louisiana law though not in conveyancing, as royalty without limiting words.

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[5]Comment (1938) 26 CALIF. L. REV. 359.
[6]Levy, *Oil Royalties—A Distinct Species of Property* (1938) 11 So. CALIF. L. REV. 319, 323.
[7]Comment (1937) 25 CALIF. L. REV. 226, n. 39.
[8]192 La. 1, 187 So. 35 (1939).
[9]187 So. at 40.
[10]*Ibid.*

Rent Royalty

So far as the rent classification of royalty is concerned, Louisiana is in accord in a general way with the rest of the jurisdictions. "In most jurisdictions royalties to accrue under a lease are considered to be in the nature of rent. . . . "[11] Rent has been defined by Tiffany in the following words:

> "Rent may be defined, in a general way, as a tribute or return of certain amount, which is regarded as issuing out of the land, as part of its actual or possible profits, and is payable by one having an estate in the land, as compensation for his use, possession and enjoyment of the land, or occasionally, as a charge on the land."[12]

The Louisiana Civil Code states that:

> "To the contract of lease, as to that of sale, three things are absolutely necessary, to-wit: the thing, the price, and the consent."[13]
>
> " . . . The price should be certain and determinate, and should consist of money. However, it may consist of a certain quantity of commodities, or even in a portion of the fruits yielded by the thing leased."[14]

The decisions placing royalty arising out of a lease contract in the rent category have been widely discussed and criticized.[15] The common law definition of rent as payment for a *use* of the land is not intellectually satisfying as a foundation for the analogy, as royalty is payment not for use but for consumption. The Louisiana court's decision that Article 2671[16] was applicable is also unsatisfactory, as oil or gas is *not* a portion of the *products* of the land. In the French law, products and fruits are synonomous, and a fruit of the land is "born and reborn of the soil."[17] Furthermore, the Louisiana court has properly refused in all other situations to classify oil and gas as fruits.[18] Whatever quarrels commentators may have with the rent analogy, the idea

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[11]Comment (1937) 25 Calif. L. Rev. 226.

[12]3 Tiffany, Real Property (3d ed. 1939) 524, § 876, discussed in Blake, *The Oil and Gas Lease—Part II* (1940) 13 So. Calif. L. Rev. 393, 411. See also Stone, *A Primer on Rent* (1939) 13 Tulane L. Rev. 329.

[13]La. Civ. Code (1870) Art. 2670.

[14]*Id.* at Art. 2671.

[15]Daggett, *loc. cit. supra* note 1; Blake, *The Oil and Gas Lease—Parts I and II* (1940) 13 So. Calif. L. Rev. 304, 393; Notes (1939) 46 W. Va. L. Q. 66, (1935) 45 Yale L. J. 363.

[16]La. Civ. Code (1870) Art. 2671.

[17]Daggett, *op. cit. supra* note 1, at 179, § 59.

[18]*Ibid.*

is too definitely anchored now for change in Louisiana or elsewhere, and as Mr. Blake has said:

> " . . . no sound reason has been advanced which properly precludes an acceptance of the principle that the lessor's royalty under the usual oil and gas lease possesses the legal incidents of rent. There is abundant authority for this principle in the decisions, and the works of textwriters and other researchers in the field, and the view receives inferential support from the English as well as the American mining cases. . . . "[19]

Indeed, it is remarkable that the courts have been able to fit the new and complicated legal issues arising out of the development of this great industry into an old mechanism with as few rough edges as are felt by the profession.

The *division* of rent royalty, particularly in joint leases, has caused difficulty in Louisiana, as elsewhere, often due to vague and cumbersome statements in instruments and to new leasing arrangements, as in community leases and other types of pooling agreements. A discussion of these controversies appears elsewhere,[20] however, and need not be repeated here; particularly since, as stated before, this type of royalty has been definitely placed in the rent category and presents no major variations from the rules laid down in other jurisdictions except those which necessarily occur because of the provisions of the Civil Code statutes dealing specifically with lease. There necessarily will be a variation of decisions everywhere because of such specific provisions. The Louisiana Legislature of 1938 passed an act[21] definitely stating that mineral leases are immovable property, thus vetoing the court's decision on a procedural point.[22] The 1940 Legislature of Louisiana passed an act[23] which may give rise to both practical and legal difficulties, as it states that the owner of any mineral interest, including a "royalty interest," must be made a party in any suit for partition by licitation.[24]

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[19]Blake, *The Oil and Gas Lease—Part II* (1940) 13 So. Calif. L. Rev. 393, 411.

[20]Daggett, *op. cit. supra* note 1, at 191 *et seq.*, § 61; Note (1939) 46 W. Va. L. Q. 66.

[21]La. Act 205 of 1938.

[22]Gulf Refining Co. v. Glassell, 180 La. 190, 171 So. 846 (1936). See also Amerada Petroleum Corp. v. Reese, 195 La. 359, 196 So. 558 (1940); Tyson v. Surf Oil Co., 195 La. 248, 196 So. 336 (1940); Allison v. Maroun, 193 La. 286, 190 So. 408 (1939); Daggett, *op. cit. supra* note 1, at 158 *et seq;* Daggett, *Work of the Louisiana Supreme Court for the 1939-1940 Term—Mineral Rights* (1941) 3 La. L. Rev. 303.

[23]La. Act 336 of 1940.

[24]Amerada Petroleum Corp. v. Reese, 195 La. 359, 196 So. 558 (1940); Daggett, *Work of the Louisiana Supreme Court for the 1939-1940 Term—Mineral Rights* (1941) 3 La. L. Rev. 303.

Rent royalty is well fixed in the law of Louisiana and has given relatively little trouble since the early days of the court's statement that:

> " . . . a mine or quarry, or land adapted to mining or quarrying, may be leased for a certain portion of the produce of such mine or quarry, and the fact that such portion is called 'royalty,' instead of rent, is not of the least consequence."[25]

In the case of *Shell Petroleum Corp. v. Calcasieu Real Estate and Oil Co.*[26] the court said, "It is well settled that the paying of a royalty, under a mineral *lease,* is the paying of rent. . . . "[27]

The prescriptive period fixed by the Code for rent has been applied;[28] the privilege granted a lessor for his rent has been applied;[29] the lease contract determines the share, or price, or consideration, which is rent;[30] the provisions of the Code for termination of a lease for non-payment of rent have been applied in proper cases.[31] Upon the whole, rent royalty in Louisiana presents no questions of exceptional interest because of their new or unique qualities, and hence this section need not be developed further in this paper.

Royalty Per Se

Royalty per se is a question of primary interest in Louisiana and elsewhere for at least two reasons: one, because there is great activity in the conveyancing of this interest, due to the fact that it is so widely handled by brokers in the state and out of it, as well as through the more ordinary local channels;[32] two, because its legal status is peculiar and is not yet thoroughly defined in the state and really depends as yet upon one judicial announcement, the case of *Vincent v. Bullock.*[33] The same thing could have been said not very many years ago of almost any mineral right in Louisiana or in varying degrees in any other oil and gas state. The Louisiana court defined the right and laid a foundation for the development of the mineral servitude in the case of *Frost-*

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[25]Logan v. State Gravel Co., 158 La. 105, 103 So. 526, 527 (1925).

[26]185 La. 751, 170 So. 785 (1936).

[27]170 So. at 791. Italics supplied.

[28]Board of Commissioners of Caddo Levee District v. Pure Oil Co., 167 La. 801, 120 So. 373 (1928), followed in Parker v. Ohio Oil Co., 191 La. 896, 186 So. 604 (1939).

[29]Logan v. State Gravel Co., 158 La. 105, 103 So. 526 (1925).

[30]Daggett, *op. cit. supra* note 1, at 181 *et seq.,* § 59.

[31]Tyson v. Surf Oil Co., 195 La. 248, 196 So. 336 (1940).

[32]Daggett, *op. cit. supra* note 1, at 191; Glassmire, Law of Oil and Gas Leases and Royalties (2d ed. 1938) 265, 266.

[33]192 La. 1, 187 So. 35 (1939), cited *supra* note 8. See also Daggett, *op. cit. supra* note 1, at 173 *et seq.,* § 58; Moses, *The Prescribability of Royalties in Louisiana* (1939) 14 Tulane L. Rev. 520; Comments (1939) 1 La. L. Rev. 416, (1939) 13 Tulane L. Rev. 279.

Johnson v. Sallings Heirs,[34] set up certain articles of the Civil Code as guide posts, and in a relatively short period of time channelized the thoughts and actions of the bar so that this type of mineral interest might be handled practically and satisfactorily. At this time the royalty right defined in *Vincent v. Bullock* may only be discussed, analyzed, analogized, compared, and speculated about; and the writer of this paper can only hope to present a few of the probable or even possible legal lanes down which this idea may wind and certainly does not assume the ambitious function of answering any of the wayfarers' inquiries regarding direction, because the court might find a better road to travel than originally charted and change its course. It may be said, however, that *Vincent v. Bullock* has been cited by the court no less than six times—three times by the author of the original opinion, twice by the Chief Justice, and once by a third member of the court.[35]

The continued reference to *Vincent v. Bullock* would certainly indicate that there is no present doubt in the minds of the justices that the principles announced in the case are satisfactory. In but one of these subsequent cases is royalty a real issue. In the latest decision, however, the following strong statement appears:

> "At that time the much debated question of prescription and interruption of prescription against royalty interest had not been decided by this Court in Vincent v. Bullock, 192 La. 1, 187 So. 35."[36]

The *Vincent v. Bullock* case held that royalty per se, unattached and not subject to an existing lease, is a real right running with the land but subject to the prescription of ten years *liberandi causa;* that this real right or obligation is a conditional one, suspensive and dependent upon the happening of the uncertain event of production; that royalty is not a servitude, not a rent charge, but a new form of real right. The term said by the court, to be set by law, during which this uncertain event, production, must take place is ten years, though Article 2038 states that, "If there be no time fixed, the condition may always be performed, and it is not considered as broken, until it has become

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[34]150 La. 756, 91 So. 207 (1922).

[35]Justice Fournet, who wrote the opinion in Vincent v. Bullock has referred to it in Amerada Petroleum Corp. v. Reese, 195 La. 359, 196 So. 558, 562 (1940); Pelican Well and Tool Supply Co. v. Johnson, 194 La. 987, 195 So. 514, 517 (1940): State *ex rel.* Bourgaux, 192 La. 95, 187 So. 66, 68 (1939). Chief Justice O'Niell has referred to that opinion in the cases of Hightower v. Maritzky, 194 La. 998, 195 So. 518, 521 (1940) and Munn v. Wadley, 192 La. 874, 189 So. 561, 563 (1939). Justice Higgins made reference to it in the case of Brown v. Sugar Creek Syndicate, 195 La. 865, 197 So. 583, 591 (1940).

[36]Brown v. Sugar Creek Syndicate, 195 La. 865, 197 So. 583 (1940).

certain that the event will not happen."[37] The contract out of which this litigation arose purported to *reserve* from a land sale a *perpetual* royalty, but the court apparently reasoned that since the right to produce could be reserved under our law but for ten years, the right to proceeds to issue from this right could last no longer. Since full power to produce went, under the contract involved, to the purchaser of the land, it might well be argued that the servitude passed also with only the outstanding burden in the reservor to receive his percentage of the proceeds, which under the doctrine of suspensive obligations might "always be performed."[38] However that may be, the court has clearly and, in the writer's opinion, wisely declared that the law sets a term of ten years during which this event, production, must happen, and otherwise "the condition is considered as broken, when the time [ten years] has expired without the event having taken place."[39]

The Louisiana court carefully avoided the error into which California fell by creating an interest not intended by the contracting parties. Since the right to search was not given to the reservor of royalty in the instrument under consideration in *Vincent v. Bullock,* the court refused to place this royalty in the servitude class, which carried the right to search.

In *Callahan v. Martin*[40] the California court:

> "1. . . . indiscriminately used the word royalty in its two senses mentioned in the text and held simply that a conveyance of a fraction of the oil to be produced in perpetuity is a conveyance of a profit a prendre in fee.
>
> "2. . . . was doing away with all distinctions between profits a prendre and royalty interest properly so-called; that is, that the owner of a royalty interest has, besides the right to receive a share of the 'rent,' the right to drill, and to participate in new leases."[41]

In criticizing the holding in this case, Mr. Robert J. Blake said:

> ". . . the supreme court, in *Callahan v. Martin,* held that a *landowner's royalty* is in the nature of a *profit a prendre,* and that therefore the holder thereof is a tenant in common with a lessee under a lease created subsequent to his interest, with an implied right of entry to go upon the premises and

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[37] La. Civ. Code (1870) Art. 2038.
[38] *Ibid.*
[39] *Ibid.* See also Vincent v. Bullock, 192 La. 1, 187 So. 35, 42 (1939).
[40] 3 Cal.(2d) 110, 43 P.(2d) 788 (1935), discussed in Blake, *The Oil and Gas Lease—Part II* (1940) 13 So. Calif. L. Rev. 393, 416.
[41] Comment (1937) 25 Calif. L. Rev. 226, n. 39.

> exercise his proportionate interest in the exclusive right to produce oil and gas. While this decision contains an excellent dissertation on the nature of the oil and gas lessee's interest, it is submitted that the designation by the court in that case of the *landowner's royalty* as a *profit a prendre* is supported neither by the terms of the instrument nor the intent of the parties."[42]

Mr. Blake said also:

> "Perhaps the reference of the court in the Callahan case to the holder of a landowner's royalty as a tenant in common arose from the court's concern for the royalty holder's position with reference to compelling reasonable development for oil and gas. In the event that the landowner, in such a situation, refused to lease the premises or develop them himself, it would seem that the holder of a landowner's royalty might be adequately protected without classifying him as a tenant in common in the exclusive right to explore for and produce petroleum."[43]

The Louisiana court in *Vincent v. Bullock* refused the plea of counsel that this type of royalty was a rent charge and outweighed their fears, if any, regarding the difficulties to be encountered by the royalty owner by their concern for the land tenure policy of the state. The royalty owner is further burdened because of the relatively short life of his interest; and yet, as Mr. Blake pointed out, there are other ways in which he may be adequately protected, and the Louisiana court will undoubtedly provide a way whether it be as suggested in this paper or not.

What *is* it then that a royalty purchaser or reservor gets when he becomes an owner of this supposedly valuable interest? Certainly not a pig in a poke nor a new kind of gold brick peculiar to Louisiana.

Generally, rules of the prescription *liberandi causa* are applicable in cases when the creditor or obligee has a right which he can enforce against the debtor or obligor but which he fails to exert. Yet, the royalty owner seems to occupy a passive position. It is clear that the royalty owner has no right to drill or to lease under this type of contract; yet the ten year prescription *liberandi causa* runs against him.

What is his position under the law of suspensive conditional obligations? Conditions suspensive are further divided under Article 2022 into casual, potestative, or mixed. The suspensive condition under con-

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[42]Blake, *The Oil and Gas Lease—Part II* (1940) 13 So. Calif. L. Rev. 393, 416.
[43]*Id.* at 417, n. 195a.

sideration has earmarks of being in the potestative class.[44] The owner of the land is the obligor, upon whom lies the duty to pay the royalty in the event of production within ten years. It cannot be said that upon him lies the duty to *produce,* since that may be impossible. His burden is only to pay in the event of production. Does the duty lie solely within his will and hence write into the contract a potestative condition?[45] Could it be said that the event[46] of production is one which is in the power of the obligor[47] "to bring about or to hinder"?[48] Since he has the sole power to explore or to lease to another for the purpose of exploration, the only way in which the event of production could be brought about, the situation smacks strongly of potestativeness. However, a long line of cases has established the fact that when one of the parties has relied upon the validity of the contract, has altered his position to his detriment, has gone forward under the agreement, any original nullity due to the potestative quality of the condition is cured.[49] In the case under discussion the obligee gave title to his land together with that member of full ownership, the servitude, reserving the royalty. Presumably, he must have received less for his land by reserving the royalty than he would have obtained for it without this burden. He has performed in as much as he can his part of the contract. Furthermore, the court has definitely declared the obligation to be suspensively conditional *only,* with no suggestion that a potestative element was ever present; and in any case it would be manifestly absurd to conclude that valid dealings in mineral royalty are impossible under Louisiana law. The analysis must proceed, if at all, under the theory that the contract is not null because of a potestative condition.

What then is the duty of the obligor, if any? It might be said that he is under no duty; that, in effect, he obligates himself *not* to produce, with a penalty in the event that he does produce. Could any benefit be said to flow to the royalty owner under this analysis? A case might be supposed, as of an adjoining landowner, where it would be beneficial not to have production. A residential area might be interested in prevention of exploration. These hypotheses are entirely artificial, however, as it is well known that royalty purchasers or reservors are interested in production. They may be, and very often are, non-resident investors. Article 2037 clearly states that, "Every condition must be performed

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[44]Brown, *The Potestative Condition in Louisiana* (1931) 6 Tulane L. Rev. 23.
[45]See Conques v. Andrus, 162 La. 73, 110 So. 93 (1926).
[46]La. Civ. Code (1870) Art. 2024.
[47]*Id.* at Arts. 2034-2036.
[48]La. Civ. Code (1870) Art. 2024, cited *supra* note 46.
[49]Daggett, *op. cit. supra* note 1, at 131 *et seq.,* § 35.

in the manner that it is probable that the parties wished and intended that it should be."[50] Of course, it may be argued that the landowner's interest in his own gains from production will be a sufficient urge to induce him to make a real effort to secure production. If, however, he has disposed of all of the royalty which he might reasonably expect to get out of a prospective lessee, then his chance of further reward will lie in having the ten years go by without production so that he may be relieved of the burden of payment in the event of production. He will look for profit in the reversion to him of this real right which the court has declared to be one which runs with the land. This hypothesis is no idle one, for many cases in conveyancing may be cited where landowners have sold all the royalty and more than they could hope to receive from a lessee.[51] Of course, it would appear that the landowner would still be entitled to an option price on land rentals, but they are comparatively negligible to the returns from production.

Conditions suspensive in the Civil Law are the same as conditions precedent in the Common Law. Mr. Justice Fuller of the Supreme Court of the United States declared in the case of *City of New Orleans v. Texas & Pacific Railway Co.*[52] that, "The suspensive condition under the Louisiana Code is the equivalent of the condition precedent at common law."[53] For that matter, in Article 2013 are found these very words, "These conditions are either conditions precedent, which suspend the operation of the contract until they are performed. . . . "[54]

The concept of conditional obligations comes from the Roman Law. Gaius said, "A condition is said to be suspensive, when the commencement of a legal transaction is made dependent upon it. . . . "[55]

These Louisiana Code articles were taken, of course, from the French Code. From *all* of these sources comes the principle that in an obligation conditionally suspensive or precedent the obligor may do nothing to prevent or hinder the happening of the uncertain event. After all, that is but simple common sense and justice, and even without specific authority might well be drawn from the four corners of any system of law.

Common Law sources state the principle this way:

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[50]La. Civ. Code (1870) Art. 2037.
[51]See Brown v. Sugar Creek Syndicate, 195 La. 865, 197 So. 583 (1940).
[52]171 U. S. 312, 18 Sup. Ct. 875, 43 L. ed. 178 (1897).
[53]*Id.* at 319, 18 Sup. Ct. at 882, 43 L. ed. at 186.
[54]La. Civ. Code (1870) Art. 2013.
[55]Tomkins and Lemon, translators, The Commentaries of Gaius on the Roman Law (1869) 184.

> "Where a contract is performable on the occurrence of a future event, there is an implied agreement that the promisor will place no obstacle in the way of the happening of such event, particularly where it is dependent in whole or in part on his own act. . . . "[56]

Article 2040 of the Louisiana Civil Code of 1870 appears in these words:

> "The condition is considered as fulfilled, when the fulfillment of it has been prevented by the party bound to perform it."

A Supreme Court Justice in the 1832 decision of *Walls v. Smith*,[57] dealing with a bond, rejected this recitation as a mistranslation which he thought might lead to "absurd consequences" and declared that the "obvious sense of the French text is, that the condition is considered as accomplished, when the debtor, whose obligation depends on this condition, prevents the accomplishment of it."[58]

Chief Justice O'Niell speaks of the Louisiana Code's translation from the French text as "incomplete and inaccurate" and states that the "French text of the article (2035) of the Code of 1825 . . . [Article 1178 of the French Code] means that the condition is considered fulfilled, when it is the debtor, bound under that condition, who prevents the fulfillment."[59] He says further that, "The error in the translation was observed long ago, and the French text has always prevailed in the decision of this court. Walls v. Smith, 3 La. 498; Rightor v. Aleman, 4 Rob. 45; Morrison v. Mioton, 163 La. 1072, 113 So. 456, 459; Kock v. Emmerling, 63 U. S. (22 How.) 74, 16 L. ed. 292."[60]

This salutary principle has been frequently resorted to by Louisiana courts. The case of *Rightor v. Aleman*[61] is an early illustration of the application of Article 2040 of the Louisiana Civil Code of 1870. The plaintiff was a surveyor who performed a professional service for the defendant for which the latter gave his promissory note for $1,000. The plaintiff signed a receipt, which appears in the following language:

> "Received of Mr. F. Aleman his note for one thousand dollars, it being the price agreed upon for the surveying of

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[56]13 C. J. 648, § 722. See also Mock v. Trustees of First Baptist Church of Newport, 252 Ky. 243, 67 S.W.(2d) 9 (1934); ANSON, PRINCIPLES OF THE LAW OF CONTRACT (Corbin's 5th Am. ed. 1930) 438; Corbin, *Supervening Impossibility of Performing Conditions Precedent* (1922) 22 COL. L. REV. 421.

[57]3 La. 498 (1832).

[58]*Id.* at 501.

[59]See Southport Mill v. Friedrichs, 171 La. 786, 132 So. 346, 348 (1931).

[60]*Ibid.*

[61]4 Rob. 45 (La. 1843).

> the land sold by the heirs of P. Aleman to La Ferriere. Now it is agreed that should the survey of mine not be sustained by the courts, then I am to deliver up said note to F. Aleman; but should it be sustained, then it is to be paid in full. A. F. Rightor."[62]

The defendant and his coheirs effected a compromise, without awaiting a trial of the case alluded to in the receipt. They thus "rendered impossible the fulfillment of the conditions contained in the receipt delivered by the plaintiff; the defendant's obligation to pay thereby became perfect, and he cannot be permitted to say the consideration had failed. Civil Code, Art. 2035."[63]

The Supreme Court of the United States in 1860 applied the principle in *Kock v. Emmerling,*[64] a suit to recover a broker's commission from a client who simply refused to complete a sale after all arrangements had been made by the dealer. The court said, "It would be a novel principle if the vendor might capriciously defeat his own contract with his agent by refusing to pay him when he had done all that he was bound to do."[65]

The case of *Lloyd v. Dickson*[66] presented a contract for joining efforts to control an insurance company of which the plaintiff was to be manager. Defendants subsequently entered into a contract with a third party, competitor of plaintiff, to negotiate and benefit from the same scheme. Plaintiff sued for damages. Defendants offered in support of a plea of exception of no cause of action, that the obligation was suspensively conditioned upon the control of the company being secured, and that it was not alleged that control was secured. The court, in overruling the exception and remanding the case for trial, said that "the obligation of defendant was not to control the company, or to secure the position for plaintiff; but only to endeavor to do both."[67] They then applied Article 2040 and said, "If instead of standing loyally by their contract with plaintiff the defendants enter into a contract destructive of it, the condition, as a matter of course, can never be fulfilled. . . . "[68]

This case seems partially to fit the new situation. There was no absolute promise to control the company but to *endeavor* to do so,

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[62] 4 Rob. 45 (La. 1843).
[63] *Id.* at 46.
[64] 63 U. S. 70, 16 L. ed. 292 (1860).
[65] *Id.* at 74, 16 L. ed. at 294.
[66] 116 La. 90, 40 So. 542 (1906).
[67] *Ibid.*
[68] *Ibid.*

and while it is *not* clear what would have been judicially considered a reasonable effort to do so, certainly some affirmative duty was laid upon the obligor in addition to the negative one not to put it beyond his power to meet his obligation by actually starting negotiations detrimental and contrary to it.

The most frequent application of the principle seems to be (as in the previously cited United States Supreme Court case of *Kock v. Emmerling*[69]) in regard to the prevention of a broker's realization of his promised commission by a refusal of the landowner to sell when a prospect has been found or by selling on his own hook to a third person without the broker's knowledge or consent;[70] these cases are thoroughly familiar to the profession and it would be tedious to recite them.

The case of *New Iberia Sugar Co. v. Lagarde*[71] presents an interesting analogy for the oil problem under discussion. In this case the plaintiff sued to recover damages in the sum of $26,000 for alleged breach of contract. The contract in question was to the effect that plaintiff, a sugar refining company, bound itself to buy cane from the defendant, a cane grower, for a five year period at so much per ton. The defendant sold his plantation with no mention of or arrangement for the carrying out of the contract, thus committing an active breach and making it impossible for him to perform. The court awarded damages based on the refining company's losses in not being able to get cane to grind, *etc.* The court stated that by this contract the cane grower "obligated himself to grow and deliver the cane on his plantation for a fixed period of time, in his name as owner, and deliver it to plaintiff as stipulated," and that his failure to do so "was a breach for which he [was] liable in damages."[72] The court said further that, "The contract entered into between the parties had all the elements to make it legal. There was a definite price. The parties to it had agreed upon all its terms and conditions. There was a defined thing to be delivered by one and paid by the other."[73] In the royalty sale or reservation the landowner certainly could not be said to have obligated himself to *produce* oil, but is there not an implied obligation to make a reasonable *effort* to secure production by leasing or attempting to lease to a reliable company?

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[69]63 U. S. 70, 16 L. ed. 292 (1860), cited *supra* note 64.

[70]See Southport Mill v. Friedrichs, 171 La. 786, 132 So. 346 (1931); Luckett Land and Emigration Co. v. Brown. 118 La. 943, 43 So. 628 (1907).

[71]130 La. 387, 58 So. 16 (1912).

[72]58 So. at 19.

[73]*Ibid.*

In the case of *Owens v. Muslow*[74] plaintiff and defendant entered into an option agreement whereby plaintiff paid $50,000 cash for the option and promised $100,000 for a later date, and defendant bound himself to deliver to plaintiff a deed to certain oil properties for the agreed price of $1,300,000 less the $150,000 paid, "provided that plaintiff should furnish defendant, on or before January 15, 1920, security or guaranty *satisfactory to defendant* for the payment to defendant of $1,150,000 on January 15, 1922, with interest at 5 per cent. per annum, payable annually."[75]

The plaintiff declined to avail himself of the option and abandoned it three days before its expiration; five years later he brought suit for the return of the option money, alleging among other things that the defendant was not bound to deed the property to plaintiff unless satisfied with the security which plaintiff might tender him. The court disposed of plaintiff's contention by pointing out that he, and not the defendant, made the performance of the condition impossible by abandoning the option and failing to submit any security at all to defendant with which he could be satisfied or dissatisfied. The court said further:

> "Now the contract before us may have been a harsh one for plaintiff, but it was not a mere nudum pactum. For it did put certain obligations on defendant.
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> "First of all it imposed on defendant at least a *natural* obligation, 'binding in conscience and according to natural justice (R.C.C. Art. 1757, No. 2),' to consider honestly the security which plaintiff might offer him and to accept that security if unquestionably sufficient to secure his debt, under pain of forfeiture of his good name, which every man pledges for the performance of those obligations which bind him in conscience. And we think further that defendant, *having received a valuable consideration* for the option, would have been legally bound to accept any security with which a reasonable man ought to have been satisfied. . . . "[76]

The last passage seems peculiarly fitting in a consideration of the problem under discussion because the primitive owner of the land in any case, having this real burden running with it, must be, in the language of Justice St. Paul, under an obligation "binding in conscience"[77] at least to accept a lease. If it could be proved that a landowner refused

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[74]166 La. 423, 117 So. 449 (1928).
[75]117 So. at 449.
[76]*Id.* at 450.
[77]La. Civ. Code (1870) Art. 1757. See also Owens v. Muslow, 166 La. 423, 117 So. 449 (1928), cited *supra* note 74.

to subscribe to a reasonably advantageous lease contract, might it not be said by a royalty owner that he prevented the happening of the condition?

An affirmative duty has been implied in lease contracts. One author has said:

> "Quite generally, when oil is discovered, the lessee is under an implied duty reasonably to develop the rest of the land leased. Under a lease for no specific term of years, the so-called 'no term' lease, such a duty attaches within a reasonable time after execution of the instrument. Under any kind of lease, where the leased land is in danger of being drained by operations upon adjacent lands, the courts have commonly implied a duty in the lessee to drill offset wells. A failure to fulfill the implied obligation under any of the above situations suffices to establish a forfeiture and to permit the lessor to maintain an action of ejectment."[78]

The second edition of Professor Merrill's work on *Covenants Implied in Oil and Gas Leases* contains a chapter on "Implied Covenants between Others than Lessors and Lessees."[79] The cases imposing upon the grantee the duty of diligent exploration are numerous in situations analogous to, though of course not identical with, the one under discussion.[80] The case of the sublessor's reserving overriding royalty[81] presents an interesting parallel, as his sole interest is in production, as is that of the owner of Louisiana royalty per se, since he has no other interest in the land, nor has he the right to search or control. However, implied duty in leasing contracts is not looked upon with too much favor by the Louisiana courts;[82] the whole legal theory of royalty per se is, of course, entirely different, and relief must be sought under the law of conditional obligations.

An affirmative idea of duty is suggested in the *Vincent v. Bullock* case in this passage:

> "Others argue that when the landowner grants a real interest to a third party, because of the nature of such an obligation, there is an implied obligation growing out of the contractual relation of the parties that the grantor or his heirs or assigns

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[78]Note (1938) 24 WASH. U. L. Q. 91, 101.

[79]MERRILL, THE LAW RELATING TO COVENANTS IMPLIED IN OIL AND GAS LEASES (2d ed. 1940) 184, c. IX.

[80]*Id.* at 409.

[81]Johnson v. Moody, 168 La. 799, 123 So. 330 (1929).

[82]See DAGGET, *op. cit. supra* note 1, at 101, § 30. See also Monroe, *The Implied Resolutory Condition for Non-Performance of a Contract—Parts I and II* (1938) 12 TULANE L. REV. 376, 509.

> will use the land with reference to the royalty as a prudent administrator and that as such it is incumbent upon the owner to lease the lands for mineral development when an opportunity to do so presents itself and can absolve himself from the application of the prescription liberandi causa only by showing that he had no opportunity to lease the premises for mineral development.
>
> "As stated above, unlike the owner of a servitude, there is no obligation on the part of the royalty owner to explore for and develop the minerals and it necessarily follows that the obstacles referred to in Article 792 of the Revised Civil Code are not applicable."[83]

The suggestion was apparently made under argument advancing the servitude doctrine of obstacle preventing the running of prescription; and, of course, the court very properly disposed of it by stating that the doctrine of servitude did not apply, as the right in litigation was *not* a servitude. Hence, it may be said that the plea of an affirmative duty under this line of reasoning has not been placed before the court.

The *Vincent v. Bullock* case was an action in jactitation or slander of title, the object of which was to annul and cancel from the conveyance records the instrument evidencing the *reservation* of royalty. The question of *sale* of royalty has not been decided, but it would appear that the problem would be answered in a similar fashion, though a stronger case might be made for perpetual disposition of this real right by the landowner himself, who owns all the elements. Also, the question of consideration would be even more convincing. Since these questions were not at issue in *Vincent v. Bullock,* they may be still considered possibilities for future pleadings. Under the doctrine of suspensive conditional obligations, would not the landowner be bound in good conscience, as Justice St. Paul said in the case of *Owens v. Muslow,*[84] to make a reasonable effort to see that production ensues? He would certainly be obliged *not* to *hinder* or prevent the happening of the uncertain event by refusing to accept a reasonably profitable lease contract under Article 2040 and the cases outlined.

Could a royalty owner bring suit upon the refusal of the landowner to lease profitably? Probably *not,* as full leasing power is in the landowner, and the latter might properly reply that *his* judgment in leasing was to be relied upon under the contract—not that of the royalty owner—and that he was waiting for a *better* bargain. But, the court might decide

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[83]Vincent v. Bullock, 192 La. 1, 187 So. 35, 41 (1939).
[84]166 La. 423, 117 So. 449 (1928), cited *supra* note 74.

that they could objectively determine whether or not the landowner should have taken the proffered lease. Even in the case of a sale of a hope does the purchaser not have a right to have the net *cast* or the crop *planted,*[85] or upon failure of the prospective actor in the contract to move, to get his money back?

If the royalty owner waits until the ten years are over and the condition broken, what are his rights? Can he get the original consideration back, as in *Owens v. Muslow?* Can he get damages, not on the speculative proposition of how much oil he has lost, but an ascertainable sum based on the price which the landowner *refused* in an offered lease contract, as in the case of *New Iberia Sugar Co. v. Lagarde?*[86]

Do minority and interdiction suspend this ten year period during which the event of production must occur? If, indeed, it is a prescription *liberandi causa*—and the court has positively stated that it is—then these disabilities *would* suspend the prescription under Article 3554 of the Civil Code of Louisiana, which provides that:

> "Prescription does not run against minors and persons under interdiction, except in the cases specified by law."

Would suspension of a minor's or interdict's right suspend prescription against all royalty owners in a given tract of land? It has been so held in regard to the mineral right in the nature of a servitude; and the decision was grounded on the theory of the indivisibility of the servitude, the benefits of which are, however, divisible.[87] This principle, originally enunciated in the case of *Sample v. Whitaker,*[88] was reiterated in November, 1940,[89] and strengthened and extended, in that the court squarely met the issue that the fractional servitude owner deriving his right at a different date and from a separate contract than that of the minor nevertheless benefited from the minor's suspension due to the indivisible nature of the property right. The court said:

> "If a mineral servitude is a property right, though indivisible, then an undivided interest in such property may be sold and disposed of in the same manner as any other property right in an indivisible object may be disposed of, and yet the property or the property right will continue to be indivisible. The only thing that occurs is that one joint owner in an indivisible prop-

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[85]La. Civ. Code (1870) Art. 2451. See Losecco v. Gregory, 108 La. 648, 32 So. 985 (1901). See also Art. 2450, Book V, Title V, Law XI, Las Siete Partidas.
[86]130 La. 387, 58 So. 16 (1912), cited *supra* note 71.
[87]See Daggett, *op. cit. supra* note 1, at 73 *et seq.*, § 21.
[88]172 La. 722, 135 So. 38 (1931).
[89]Ohio Oil Co. v. Cox, 198 So. 902 (La. 1940).

> erty is replaced by the vendee or transferee, who then becomes a joint owner in the indivisible property in the place of his vendor."[90]

It was also true in the *Ohio Oil*[91] case, as in many contractual situations of this nature, that the mineral servitude had been divided and redivided until the fractional holdings were very small, under the statement in the decision, running to 256ths.

The argument for major *royalty* holders would be stronger than for major mineral right or *servitude* owners for at least two reasons—one, that they do not have the right to develop or lease as does a mineral right holder; two, because their right to a percentage of the proceeds accrues only upon the happening of an event (production), certainly an indivisible condition from which rights immediately accrue to all holders in the proportions of their purchase or reservation—exactly the case in the successful exercise of the servitude. The indivisibility of the event objectively and factually is more convincing than the indivisibility of the servitude, a legal postulate, laid down by a code article, the benefits of which are clearly said to be divisible.

Since the burden runs with the land, would subsequent owners be under the same duty, if any, as the original assumer of the obligation? Negative burdens running with the land are familiar, as in sales carrying the *prohibition* of subsequently selling to a negro,[92] of building a house costing less than a certain sum of money, of setting a building back from the street less than a certain number of feet, etc.[93] Under this line of cases relief may be had against subsequent owners of land as well as against the original vendee not only by the original vendor but by other vendees relying on the prohibitions against their neighbors and on the faith of which they have bought. The burden of royalty, if any, would seem to be an affirmative one, to produce or attempt to produce, or at least the doubly negative one of not *refusing* to set in motion acts which might lead to production.

In *Vincent v. Bullock* the property was transferred subject to the royalty reservation and without warranty of title, and the court said:

> "We therefore conclude that the plaintiffs, by the reservation made in the transfer of their property by deed of February

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[90]198 So. at 908.
[91]Ohio Oil Co. v. Indiana, 177 U. S. 190, 20 Sup. Ct. 576, 44 L. ed. 729 (1900).
[92]Queensborough Land Co. v. Cazeaux, 136 La. 724, 67 So. 641 (1915).
[93]Rabouin v. Dutrey, 181 La. 725, 160 So. 393 (1935); Hill v. Ross, 166 La. 581, 117 So. 725 (1928).

22, 1927, imposed on the property a real obligation which passed with the property into the hands of the present owner."[94]

Did the original vendee of the land and right to search pass his obligation to the royalty owner to the purchaser? Apparently he did, because he sold not only the land but the right to search, which would, under this analysis, carry with it the *duty to search.*

These and many other questions arise out of this landmark decision, and we may await the judicial or legislative answers with deep intellectual curiosity, as this new idea must stir the imagination of all who are interested in royalty. That the owner of the right to search cannot deliberately and unnecessarily refuse to act without suffering a consequence seems to be certain. That he cannot be expected to perform a miracle is certain. Between these points his duty seems doubtful and must depend upon peculiar facts. If he loses money himself by exercising what later appears to have been bad judgment, he can scarcely be held to have violated the contract. If he deliberately awaits the expiration of the ten year period to begin his search and materially profits thereby, his behavior might be said to be fraudulent, whatever the law of conditional obligations. Proof of intent would, of course, be difficult, as always. The owner of royalty per se must have some protection for his money placed in a legitimate venture.[95] The exact relief will be pointed out by the court in perhaps the very near future.

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[94]Vincent v. Bullock, 192 La. 1, 187 So. 35, 40 (1939).

[95]48 STAT. 881 (1934), 15 U.S.C.A. § 78 (Supp. 1940). See also 48 STAT. 74 (1933), 15 U.S.C.A. § 7a (Supp. 1940): 48 STAT. 912 (1934), 11 U.S.C.A. § 207(h) (1937); 49 STAT. 911 (1935), 11 U.S.C.A. § 205(f) (1939); 49 STAT. 803 (1935), 15 U.S.C.A. § 79a (Supp. 1940); 49 STAT. 1375 (1936), 15 U.S.C.A. § 78 (Supp. 1940). See Bates and Douglas, *The Federal Securities Act of 1933* (1933) 43 YALE L. J. 171.

DOWER RIGHTS UNDER OIL AND GAS LEASES

*W. Lewis Roberts**

Writers on the subject of oil and gas leases have given scant attention to the rights of the widow of one who has executed an oil and gas lease on his lands or of one who has received such a lease. The bulk of a deceased person's estate may consist of rights created by such leases. In such a case it becomes very important to determine what his widow's interest in such leases is. While the case of the widow of a lessor seems to have come often before the courts, the case of the widow of the lessee has seldom been passed upon. The decisions give us little help in determining just what she should receive. This may be due partly to the fact that the lessees are more often than not corporate entities. Whether that be the fact or not, the question of what rights are created in such leases as concerns the widow of either a lessor or a lessee of an oil and gas lease, is sufficiently intriguing to invite a brief study of the same.

At the outset it is necessary to bear in mind that dower, as such, has been abolished in many jurisdictions and a share in the estate of a deceased spouse has been provided for in a statute of descent and distribution; and also that in the so-called community property states, the surviving wife is taken care of under the rules of community property law. In this latter case we find the oil and gas producing states of California,[1] Louisiana,[2] New Mexico,[3] and Texas.[4] In these states the surviving spouse is usually given one-half of the community property, if there are children. If there are none, his or her share may be increased over that amount. In another group of states, dower is also abolished as such and provision made for the surviving wife in the statutes of descent and distribution. Among the leading oil producing states found in this group are Indiana,[5] Kansas,[6] Oklahoma,[7] and Pennsylvania.[8] In Indiana if a husband or wife dies intestate, leaving no child and no father or mother, the whole of his or her property, real and personal,

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[1]CAL. CIV. CODE (Deering, 1937) § 173.
[2]LA. CIV. CODE ANN. (Dart, 1932) § 915.
[3]N. M. STAT. ANN. (Courtright, 1929) §§ 68-308.
[4]TEX. STAT. (Vernon, 1936) Art. 2578.
[5]IND. STAT. ANN. (Burns, 1933) §§ 6-2353, 6-2324.
[6]KAN. REV. STAT. (1923) §§ 22-108.
[7]OKLA. STAT. (Harlow, 1931) §§ 1617, 1618.
[8]PA. STAT. (Purdon, 1936) tit. 12, § 6 and see PA. STAT. (Purdon, 1936) tit. 20, § 1.

goes to the survivor. In Kansas, the wife takes one-half of what is left of the realty after the debts are paid. In Oklahoma, if there is one child, the estate is divided between the child and the surviving spouse; if there are are two or more children, the surviving spouse has one-third only. The provision under the Pennsylvania statute is to the same effect. In a third group of states we find common law dower given as such or under statutory changes. Among the oil and gas producing states in this class are to be noted Illinois,[9] Kentucky,[10] Montana,[11] Ohio,[12] and West Virginia.[13]

Another element that must be borne in mind in dealing with a question of this kind is the fact that there are different types of oil and gas leases in common use. One authority, emphasizing the form of the granting clause, speaks of a lease as (a) a demise of the land, (b) a grant of the oil and gas, (c) a grant of an exclusive right to produce.[14] The first purports to grant the land described for the sole purpose of mining and operating for oil and gas; the second to sell and convey all the oil and gas in and under the described premises with the privilege of drilling and operating for the same; and the third grants the exclusive right to mine and produce oil and gas in the land mentioned in the lease with the right to possess and use so much of the surface thereof as may be necessary for that purpose. Another leading authority in this field stresses the provisions found in the habendum clause.[15] He points out that the form of the lease used has varied in the different stages of the development of the industry. Originally the lease was given for a definite term of years. This might be for a long term. Then an option for the renewal of the lease was added. Finally to the definite term was added the provision that the lease should last so long after the term mentioned as oil or gas should be produced in "paying quantities." This was spoken of as the "thereafter" clause. Then the "no term" lease was developed with a "drill or pay" clause together with a "surrender" or "unless" clause, which mark the modern lease. These provisions as to the obligation of the lessee to drill a well or to pay rentals supply a third basis for the classification of oil and gas leases.[16]

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[9]Ill. Rev. Stat. (1937) tit. 41, § 1.
[10]Ky. Stat. Ann. (Carroll, 1936) § 2132.
[11]Mont. Rev. Codes Ann. (Anderson & McFarland, 1935) §§ 5813-5821.
[12]Ohio Gen. Code Ann. (Page, 1937) §§ 10502-1—10502-8.
[13]W. Va. Code Ann. (Mitchie & Sublett, 1937) § 4096.
[14]Mills & Willingham, Law of Oil and Gas (1926) 42.
[15]2 Summers, Oil & Gas (Perm. ed. 1938) c. 10.
[16]Walker, *Property Interests Created by an Oil and Gas Lease in Texas* (1928) 7 Tex. L. Rev. 1, 11.

A further difficulty is met at the start of our investigation of this problem in the fact that the instrument by which interests in oil and gas are created have been termed "leases." As has been pointed out by an earlier writer on the nature of oil and gas leases, courts have frequently assumed that a tenancy was thereby created and that the rules governing the relationship of landlord and tenant applied to a certain extent.[17] This is noticeable in the treatment of royalties as rent and the allowing of the apportionment of the same when the reversionary interest is severed; and also in the application of statutory provisions for treating an indefinite term as a tenancy from year to year to oil and gas leases. The mistake in so treating oil and gas leases is evident when we recall that under a lease of a term of years the lessee cannot take away the soil or any parts thereof, while in the case of the so-called oil and gas lease that is just what the grantee is supposed to do. The lessee of a term is thereby given the use of the land for a certain period; the lessee under an oil and gas lease is given more, a part of the substance of the land itself.

In considering what dower rights are created under oil and gas leases, let us first see what the decisions show in regard to the rights of the widow of the lessor.

Dower Rights of the Lessor's Widow

Since both oil and gas are classified for legal purposes as minerals,[18] it was the natural thing for courts to look at the decisions regulating rights in mines and other minerals to aid them in solving problems affecting interests in oil and gas. By the time such problems began to appear, the dower rights of a surviving wife in the reversionary interests of a lessor of mining property were well worked out. At common law it was well settled that dower existed in mines that had been opened in the husband's lifetime, and it was equally well settled that the widow could not open new mines in lands alloted to her as dower. For her to do so would make her liable to the remainderman for waste.[19] Where mines had been opened under an enforceable lease executed by the husband before his decease, it was said that the former owner of the fee had impressed the character of mining land upon the property before

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[17]Simonton, *The Nature of the Interest of the Grantee under an Oil and Gas Lease* (1920) 26 W. Va. L. Q. 295, 321.

[18]Westmoreland & Cambria Nat. Gas Co. v. De Witt, 130 Pa. 235, 18 Atl. 724 (1889).

[19]Daniels v. Charles, 172 Ky. 238, 189 S.W. 192 (1916); Kentucky River Consolidated Coal Co. v. Frazier, 161 Ky. 374, 170 S.W. 986 (1914).

the commencement of the life term, although mines had not been opened thereunder until after the beginning of the life estate.[20]

Where mines were opened pursuant to rights granted by the widow and remainderman after the husband's death, the Kentucky court held that the widow was entitled to interest on one-third of the royalties during her lifetime under the statute in force in that state.[21] The Illinois court, in giving the widow dower in mines opened by the reversioner, said that the heir in opening such mines had destroyed all other profits of the land, except working the mines, and that unless the widow were allowed to work the mines, the land would be profitless to her.[22] The same court allowed a widow who had been assigned dower in land subject to a mining lease executed by her husband and herself to receive all payments under the lease although the mines had not been opened at the time of the assignment of dower.[23] The royalties received under mining leases were treated as substituted for the land itself just as at common law rent was treated as a substitute for the land; and a widow was allowed a third of such royalties from leases made by the husband before his death.[24]

The royalties received from wells opened before the death of the husband on lands of which he was seised, or opened after his death under enforceable contracts entered into before his death, are likewise deemed real estate of which his widow is dowable.[25] In support of this position, one decision contains an excerpt from Scribner on *Dower* to the effect that an estate for years, whether entered into before or after marriage or whether joined in by the wife, presents no obstacle to her claiming dower of the reversion in fee and also to a proportionate part of the rent as incident to the reversion.[26]

Now if the widow is entitled to share in the royalties derived from oil and gas wells, the question naturally arises as to the proportion of such royalties to which she is entitled. Is she entitled to one-third the amount received as royalties from the wells opened on the land of which she is dowable or to one-third the interest or income derived from the fund produced by the payment of royalties? The language used

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[20]Daniels v. Charles, 172 Ky. 238, 189 S.W. 192 (1916).
[21]Williamson v. Williamson, 223 Ky. 589, 4 S.W.(2d) 392 (1928).
[22]Lenfers v. Henke, 73 Ill. 405, 24 Am. Rep. 263 (1874).
[23]Priddy v. Griffith, 150 Ill. 560, 37 N.E. 999 (1892).
[24]Hendrix, Ex'r v. McBeth, 61 Ind. 473, 28 Am. Rep. 680 (1878).
[25]Standard Oil Co. v. J. P. Mills Organization, 3 Cal.(2d) 128, 42 P.(2d) 797 (1935); Crain v. West, 191 Ky. 1, 299 S.W. 51 (1921); Manufacturer's Light & Heat Co. v. Knapp, 102 W. Va. 308, 135 S.E. 1 (1926).
[26]Campbell v. Lynch, 81 W. Va. 374, 94 S.E. 739 (1918).

in some of the cases does not make this as clear as it might. If we consider that the royalties received are in the nature of income from the land, the widow should be given one-third of the total amount received as royalty. If the amount received is really a conversion of capital and the land is being depleted, then it would seem that she should get only the income or interest on one-third the amount received as royalties. Of course, statutory modifications on the old common law rule of dower make a difference in some jurisdictions. In *Stewart v. Tennant,*[27] the West Virginia judges said that since the statute gave her one-third of the rents, issues, and profits until dower was assigned, such rents, issues, and profits arising from oil were measured by the interest on the fund arising from its production called "royalty." The Kentucky court, in *Collins v. Lemaster's Adm'r,*[28] said that the lower court should have ascertained the present cash value of the dower right in royalties and given the widow the cash or caused the accruing amounts to be invested and the income paid to her during life. However, in the later case of *Cook v. Cook's Adm'r,*[29] the court held that after allotment of dower in the husband's real estate, she was entitled to one-third of the royalties of gas wells absolutely throughout life and not merely to the income from such one-third. In this case a lower court had made a division of the farm and it did not appear that any wells had been drilled on the part alloted to the widow. The court said that she was entitled to one-third the royalties irrespective of whether wells were located on the part assigned her or not. The court pointed out that some jurisdictions do not apportion the royalties where there has been a division of the land, after an oil and gas lease has been executed thereon, but allow each person the royalties derived from wells drilled on his part.[30] Where the wife claimed her homestead right in lands of her husband on which he had executed oil leases without her joining therein, the Kentucky court held that she had a dowable interest in royalties from oil and gas leases until dower was assigned and allowed her administrator to collect her portion of such royalties to the time of her death.[31] Under the Texas statute, which reaches a result somewhat similar to that reached at common law, it was held that a wife upon surviving her

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[27]52 W. Va. 559, 44 S.E. 223 (1903).
[28]232 Ky. 188, 22 S.W.(2d) 567 (1929).
[29]261 Ky. 501, 88 S.W.(2d) 27 (1935).
[30]Osborn v. Arkansas Territorial Oil & Gas Co., 103 Ark. 175, 146 S.W. 122 (1912); Fairbanks v. Warrum, 56 Ind. App. 337, 104 N.E. 983 (1914); Northwestern Ohio Nat. Gas Co. v. Ullery, 68 Ohio St. 259, 67 N.E. 494 (1903); Pierce Oil Corp. v. Schacht, 75 Okla. 101, 181 Pac. 731 (1919); Kimbley v. Luckey, 72 Okla. 217, 179 Pac. 928 (1919).
[31]Bartlett v. Buckner's Adm'r., 265 Ky. 747, 97 S.W.(2d) 805 (1936).

husband acquired a life estate in one-third of the land of which he was seised during the marriage, and was therefore entitled to one-third of the one-eighth mineral royalty that had been reserved on the entire tract.[32] The New Mexican community property law gives the husband full management of the community property with power to dispose of the personalty. To convey the realty, there must be a joinder of the wife in the conveyance. There it is held that a lease of the oil and gas rights which is given for a period of five years and as long thereafter as oil and gas are produced by the lessee, is void unless the wife joins therein. This shows that such a lease creates more than a chattel real.[33]

In a Pennsylvania superior court case, it is interesting to note that the execution of a will devising the land on which the testator had previously given an oil and gas lease, worked an ademption of the right to the royalties payable under the lease on wells operated on the devised property.[34] A father willed the land in question to his son upon condition that the son pay his executors the sum of five thousand dollars.

From the authorities we have thus far considered, it seems to be fairly well established that the widow of a lessor of an oil and gas lease is dowable in royalties received thereunder. When we turn to the case of the widow of the lessee, we do not find the law as clearly marked out.

Dower Rights of the Lessee's Widow

In order to determine what dower rights the widow of a lessee should have, it is first necessary to determine the nature of the interest created in the lessee under an oil and gas conveyance. There are two views as to this interest; one being that oil and gas can be owned in place just as solid minerals and the other that they cannot be so owned, that ownership is not acquired in them until they are reduced to possession by being brought to the surface and placed in retainers. This latter view is known as the non-ownership theory of oil and gas law. Texas has been the most outspoken advocate of the ownership theory and holds that the lessee may acquire an estate in oil and gas in place apart from the ownership of the surface.[35] It should follow then that if the lease be not for a definite term of years but for an indefinite period, as long "thereafter as oil and gas is produced in paying

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[32]Belote v. Brown Securities Corp., 129 S.W.(2d) 395 (Tex. Civ. App. 1940).
[33]Terry v. Humphreys, 27 N. M. 564, 203 Pac. 539 (1922).
[34]Prager's Estate, 74 Pa. Super. 592 (1920).
[35]Texas Co. v. Daugherty, 107 Tex. 234, 176 S.W. 717 (1917).

quantities," the widow of the lessee should have dower in the estate so created by the lease. The estate created by the lease is, according to the Texas view, a corporeal hereditament, and Kent tells us that "dower attaches to all real hereditaments, such as rents, commons in gross or appendant, or piscary, provided the husband was seized of an estate of inheritance in the same."[36] As we have already seen, in Texas the rights of the surviving spouse are fixed by statute, which gave him or her one-third of the lands of the intestate for life; so it is held that the life tenant's right in oil extends only to interest for life on one-third the proceeds from the sale of oil and that the principal goes to the remainderman.[37]

Courts in several of the other jurisdictions where oil and gas problems come before them, have said that the interest created by an oil lease is a profit a prendre, an incorporeal hereditament.[38] A profit a prendre has been defined as the right to take part of the soil or the products of the soil from the land of another. It differs from an easement in that an easement permits the use of another's land or restricts the uses an owner may make of his land; while a profit allows the taking of something from another's land.[39] Both are alike in respect to their acquisition; either may be gained by express grant or by prescription.[40] Tiffany says:

> "A right to take oil or gas from land in which the person so entitled has no right or ownership is likewise, though not always expressly so stated, a right of profit a prendre. 'Under the usual oil and gas lease,' it has been said, 'the owner-lessor transfers to his lessee his right to drill for and produce oil and other substances. The rights of the lessee present a clear case of profit a prendre in gross, a right to remove a part of the substance of the land.' And in such case, the lessee has an interest in the land in the nature of an incorporeal hereditament. Frequently what is properly a profit a prendre as regards minerals in land, that is, a power of a more or less permanent char acter to take as one's own minerals in the land, is referred to as a mining license, the important distinction, before referred to, between a profit a prendre and a license, being thus ignored."[41]

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[36]3 KENT COMM. *41.

[37]Higgins Oil & Fuel Co. v. Snow, 113 Fed. 433 (C.C.A. 5th, 1902); also Swayne v. Lone Acre Oil Co., 98 Tex. 597, 86 S.W. 740 (1905), citing TEX. REV. STAT. (1895) Art.'s 1689, 3256.

[38]Phillips v. Springfield Crude Oil Co., 76 Kan. 783, 92 Pac. 1119 (1907); Rich v. Doneghey, 71 Okla. 204, 177 Pac. 86 (1918). Also see Roberts, *Inconsistencies Under the "Ownership in Place" Theory of Oil and Gas* (1940) 29 KY. L. J. 3.

[39]MINOR & WURTS, REAL PROPERTY §§ 66, 89.

[40]3 TIFFANY, REAL PROPERTY (3rd ed. 1920) 432, § 842.

[41]*Id.* at § 847.

This right to take part of the substance of the soil of another may be an exclusive right or it may be shared with others as in the case of a right of common.[42] It may be for the benefit of a particular piece of land, that is appurtenant to land; or it may be in gross, that is for the benefit of the owner thereof without regard to the ownership of any other holding.[43] The owner's interest in a profit a prendre may be for a definite term of years, for life or for an indefinite length of time, just as in the case of easements. That is to say, there may be terms of years, life estates, fees simple or determinable fees in profits a prendre.[44] As in the case of an easement, also, a grantor, in conveying his land, may "reserve" or "except" a profit a prendre.[45] A profit a prendre carries with it the right to make such use of the surface as is reasonably necessary to its enjoyment, and the owner of the same may maintain an action of *quare clausum fregit* against one who interferes with his right.[46]

While the instruments creating rights in oil and gas are called leases and, by some of the earlier decisions in Louisiana, are held to be leases and not conveyances, more recent decisions in that state have held them to be grants of servitudes.[47] The late Professor Simonton distinguishing between a common law lease and a grant of an oil and gas right said:

> "The lessee has no right to destroy the substance of the soil unless such right be expressly conferred, but has only the right to use the premises leased. If he takes part of the soil itself he is guilty of waste. It seems clear, therefore, that the estate in land which the grantee acquires under an oil and gas lease is not a leasehold estate and that the relation of landlord and tenant does not arise between the parties. The sole object of the oil and gas lease is to search for and produce oil and gas, a thing which no tenant would have a right to do without special permission granted in his lease. The grantee under an oil and gas lease has no right in the surface of the land except those necessary to enable him to carry out advantageously the one object of the grant."[48]

He concludes that the instrument granting oil and gas rights in land creates a profit a prendre and that the estate in such profit may be

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[42] MINOR & WURTS, REAL PROPERTY § 66.
[43] *Id.* at § 67.
[44] 3 TIFFANY, REAL PROPERTY (3rd ed. 1920) 428, § 842.
[45] *Id.* at 432, § 839.
[46] *Id.* at 428, § 839.
[47] Kepper, *The Judicial Nature of Oil and Gas Rights in Louisiana* (1939) 9 TULANE L. REV. 275.
[48] (1918) 25 W. VA. L. Q. 295, 320.

for years, life or in fee simple; and that a lease to last so long as oil and gas are produced in paying quantities cannot be a term of years. He further points out that the real purpose of the lease is to develop the land in order to secure the minerals, title to which passes to the grantee when reduced to possession, a characteristic of a profit a prendre.[49]

To show that the interest created by an oil and gas lease is a profit a prendre, we do not have to rely on text writers alone. The courts have time and time again stated the fact. An early Kansas decision said: "An oil and gas lease conveys no present vested interest in the oil and gas in place. The interest conveyed is a mere license to explore—an incorporeal hereditament—a profit a prendre."[50] The Indiana court early expressed the same idea.[51] The Oklahoma court observed:

> "This right [to explore for and reduce to possession oil and gas] is the proper subject of sale . . . and held separate and apart from the possession of the land itself, is an incorporeal hereditament or more specifically, as designated in the ancient French, a profit a prendre, analogous to a profit to hunt and fish on the land of another. . . . Considered with respect to duration, if the grant be to one and his heirs and assigns forever, it is of an interest in fee. . . . An interest of less duration may be granted, and that for a term of years has been denominated by this court a chattel real. . . . Such a right is an interest in land."[52]

The recent California decisions are to the same effect. In *Callaghan v. Martin*[53] the judges state in their opinion that "These rights of the lessee present a clear case of a profit a prendre in gross, a right to remove a part of the substance of the land. If the oil and gas lessee is not granted exclusive possession of the surface by the terms of the lease, he has nevertheless a right to such possession as is necessary and convenient for the exercise of the profit, which in fact, may preclude any other surface possession." It further laid it down as the law in California that "the interest of the lessee is an estate for years and a present interest and estate in land." The same court in the same year decided the case of *Dabney v. Edwards*,[54] which raised the question of the classification of oil and gas leases as personalty or realty for the purpose of determining whether an agreement author-

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[49](1918) 25 W. VA. L. Q. 295, 322.
[50]Phillips v. Springfield Crude Oil Co., 76 Kan. 783, 92 Pac. 1119 (1918).
[51]Townsend v. State, 149 Ind. 624, 47 N.E. 19 (1897).
[52]Rich v. Doneghy, 71 Okla. 204, 177 Pac. 86, 89 (1918).
[53]3 Cal.(2d) 110, 43 P.(2d) 788 (1935).
[54]5 Cal.(2d) 1, 53 P.(2d) 237 (1935).

izing a real estate broker to sell was within the Statute of Frauds. The court there called attention to the fact that the California courts had uniformly held that an oil and gas lease created a term for years and was personalty; but that if the interest created was for an indefinite period, which the common law classified as a freehold estate in the nature of a determinable fee, it must be classed as real property. The clause providing for the continuance of the lease "as long as oil or gas may be found in paying quantities" creates such an indefinite duration as to make the interest created a freehold estate. Again in the case of *Dabney-Johnson Oil Corp. v. Walden*,[55] the California court reiterated the statement that a right to drill and operate for oil is a profit a prendre, a right to remove a part of the substance of the land, and that such profit a prendre is an interest in land in the nature of an incorporeal hereditament. The same court decided *Standard Oil Co. of California v. John P. Mille Organization*[56] in the same year that it rendered its decision in *Callaghan v. Martin*.[57] They said that the assignees of the lessor's interest in his oil rights secured rights in real property which might be enforced against the grantee of the land itself. The court considered the oil royalty as rent and refused to allow apportionment. It said that oil brought to the surface upon one of the several parcels into which the land had been divided might in fact be drawn from beneath the surface of the other subdivisions. In the *Dabney v. Edwards* case it observed that if the lease is to run for a fixed time and so long thereafter as either oil or gas is produced in paying quantities a freehold is created in the nature of a determinable fee.

It remains then for us to consider what interest a widow has in her deceased husband's oil and gas rights, which we have seen are to be classed as profits a prendre, *i.e.*, whether a widow has a dower in such interests. Of course if the estate be only for a term of years or for life, the question of dower does not arise. If it be a fee simple or a determinable fee, then the widow should be given dower unless there are statutory provisions that have supplanted the common law rule as to dower. As we have seen, dower attaches to all real hereditaments, according to Kent,[58] whether they be rents, commons, or piscaries, provided that the husband be seised of an estate of inheritance in the same. From the older decisions we find that this is true. We find the court setting off dower in a fishing privilege,[59] in the right to

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[55]4 Cal.(2d) 637, 52 P.(2d) 237 (1935).
[56]3 Cal.(2d) 128, 42 P.(2d) 797 (1935).
[57]3 Cal.(2d) 110, 43 P.(2d) 788 (1935).
[58]3 KENT COMM. *41.
[59]Wyman v. Oliver, 75 Me. 421 (1883).

quarry limestone,[60] and in iron ore beds.[61] It seems, then, that since an oil and gas lease creates a profit, if it be of indefinite duration, the widow of the lessee is entitled to dower therein.

Summary

In considering whether there are dowable interests created under oil and gas leases, we have to bear in mind that some of the leading oil and gas producing states follow the community property law rules, under which the rights of the surviving spouse are provided for; and that there are many other jurisdictions where dower has been abolished as such and provisions made in substitution thereof in the statutes of descent and distribution. A number of the so-called oil and gas states fall into this group. There are still other states where dower has been subjected to statutory modifications. We have seen also that there are variations in the forms of leases used. Some are given for definite periods of time and some to last as long as oil and gas are produced in paying quantities. The former would give a term of years and create a chattel real, not subject to dower; and the latter would create a determinable fee.

We find that the widow of the lessor is given dower in the royalties produced under leases that her husband executed. This treatment of the royalties as realty is due to the fact that the common law looked upon rents as standing in the place of the land itself and gave dower therein. The courts assumed that royalties were but another form of rents and therefore followed the same rule. A difference of opinion exists, however, as to whether the widow should be given the interest from the royalties paid or the royalties derived on her third of the land assigned under dower.

If the lease is for a term of years, it follows that the widow of the lessee should take nothing under it. If it be for an indeterminate time, it creates a real property estate. Whether the lessee's widow in such case should receive dower depends upon the nature of the right created by the lease. Text writers and the courts in many jurisdictions recognize that oil and gas leases really create profits a prendre. They give the right to take a part of the substance of the soil. Under common law principles, profits may be for a term of years, for life or in fee simple. It seems to follow, then, that if the lease is for an indefinite period, it is a determinable fee and should give the widow of the lessee a dower right.

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[60]Moore v. Rollins, 45 Me. 493 (1858); Billings v. Taylor, 27 Mass. (10 Pick.) 460, 20 Am. Dec. 533 (1830).

[61]Coates v. Cheever, 1 Cow. 460 (N. Y. 1823).

THE CONSTITUTIONAL, LEGISLATIVE AND JUDICIAL GROWTH OF OIL AND GAS CONSERVATION STATUTES

*Leslie Moses**

Basically related to the problems of legislation for the petroleum industry are the natural conditions under which oil and gas are found.

In most instances oil and gas exist in those portions of the earth's surface where shale, sandstone and limestone are encountered. These strata or rock were probably once muds, sands and limestones laid down on the ocean floor, containing quantities of animal and vegetable life. The addition of other strata of earth, or rock, created considerable weight and compressed the mud and sand into shale and sandstone. Through the medium of some unknown force, portions of the plant and animal life were transformed into oil and gas, and the pressure forced such oil and gas out of the shale into the permeable sandstone or limestone formations either above or beneath the shale beds. These deposits of oil and gas are found where entrapped; such entrapment being occasioned by an impervious barrier stopping the migration of oil and gas.

When entrapment has taken place, the oil, gas and water come to rest within the reservoir according to their specific gravities. Gas, being the lightest, occupies the highest place in the reservoir; oil being the next lightest, is in the middle; and water, being the heaviest, occupies the lowest position. Traps are porous or permeable layers of limestone or sandstone containing oil or gas, wherein farther migration is stopped because of a barrier of non-porous or impermeable material, which may consist of shales, tightly cemented sands, or dense limestone. These traps are properly called "reservoirs." Reservoirs containing oil and/or gas are mistakenly called "pools," which gives the impression that they are comparable to pools, ponds or lakes of water. The reser-

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voirs are, in most instances, under high pressure; the pressure usually is about forty pounds for each one hundred feet the reservoir lies beneath the surface of the earth. This pressure has a considerable effect upon the contents of the reservoir. It compresses the gas so that it occupies about one per cent of the space it would occupy at atmospheric pressure and it increases the amount of gas dissolved in the oil, making the oil more fluid. When a well is drilled into the reservoir the pressure necessarily drops and two important things occur. First, the gas, expanding under reduced pressure, moves towards the well hole and pushes ahead of it whatever else is found in the reservoir. Second, the gas comes out of solution in the oil and increases the viscosity of the oil, making it more difficult to move. This latter step is an important one to remember in discussing conservation.

Accordingly, when a reservoir is discovered, there are in it three things of vital importance to the producer, the oil, the gas, and the reservoir pressure. All three are of equal importance, for without pressure it is impossible to extract the oil. If the pressure is conserved and controlled, the ultimate recovery of the reservoir will be greatly enhanced. The conservation and maintenance of the reservoir pressure is accomplished by control of the production from the reservoir, proper spacing of the wells drilled into the reservoir, and repressuring, by gas or water, of the reservoir. Such steps are necessary and important for the proper conservation of the mineral resources, and the enlargement of the recovery from the reservoir.

Unfortunately the ruthless waste of oil and gas in the past has been due to the law's conception that the ownership of these minerals exists by the act of reduction to possession, as distinguished from the ownership of the minerals in place beneath the surface.

Oil and gas are migratory by nature. In the earlier days the courts had to hold that reduction to possession was the only method of determining ownership, as they could not tell, with any degree of accuracy, whether the oil migrated from under *A*'s land to the well drilled on *B*'s land; and, even if they found that it did migrate, they could not say how much had migrated. The fugacious character of the minerals led to their classification by the courts as minerals *ferae naturae*.[1] The persistence of this idea would not have been so serious if simultaneously

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[1]Walls v. Midland Carbon Co., 254 U. S. 300, 41 Sup. Ct. 118, 65 L. ed. 276 (1920); Ohio Oil Co. v. Indiana, 177 U. S. 190, 20 Sup. Ct. 576, 44 L. ed. 729 (1900); People v. Associated Oil Co., 211 Cal. 93, 294 Pac. 717 (1930), *aff'd*, 212 Cal. 76, 297 Pac. 536 (1931).

with the declaration of the doctrine some means had been devised whereby each owner would have been restricted to the taking of his proportion only of the contents of the common reservoir. If the law had recognized that each owner's proportionate part of the reservoir could have been determined before the reservoir had been exhausted, instead of being determined by a race between the owners as to who could get the most from the reservoir, the economic evils attending the doctrine would have been avoided in time. This doctrine, and the analogizing of oil and gas to wild animals, led to the formulation and establishment of the doctrine of the "Rule of Capture," the "Offset Drilling Rule" and their antithesis, the "Ownership in Place Rule."

The Rule of Capture and the Offset Drilling Rule

The Rule of Capture has been described by that eminent attorney Robert E. Hardwicke,[2] in his article "The Rule of Capture and Its Implications as Applied to Oil and Gas"[3] as follows:

> "Disregarding refinements and apart from implications or incidental corollaries, and reduced to its fundamentals, the Rule of Capture may be stated as follows: The owner of a tract of land acquires title to the oil or gas which he produces from wells drilled thereon, though it may be proved that part of such oil or gas migrated from adjoining lands."[4]

In the same article he has defined the Offset Drilling Rule as follows:

> "An owner of land which is being drained by the operation of wells in neighboring lands can not enjoin the further operation of the offending wells and can not recover damages from the operator thereof, but must protect his lines as best he can "by producing from offset wells drilled on his own lands."[5]

The belief was universal that the two rules were one and the same, or at least that the latter rule was a part of the Rule of Capture. In fact, in some instances the courts have construed the two rules together. However, one is the natural outgrowth of the other. While the phrase "Rule of Capture" is now commonly used, and its meaning seemingly fixed, the phrase itself has never been defined by the courts, and its inception is unknown. It is attributed to the following language of the Pennsylvania court in *Westmoreland Natural Gas Co. v. DeWitt*[6]:

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[2]Of the law firm of Hardwicke & Check, Fort Worth, Texas.
[3](1935) 13 Tex. L. Rev. 391.
[4]*Id.* at 393.
[5]*Ibid.*
[6]130 Pa. 235, 18 Atl. 724, 725, 5 L. R. A. 731, 732 (1889).

> "Water and oil, and still more strongly, gas may be classed by themselves, if the analogy be not too fanciful, as minerals ferae naturae. In common with animals, and unlike other minerals, they have the power and the tendency to escape without the volition of the owner. Their 'fugitive and wandering existence within the limits of a particular tract was uncertain,' as said by Chief Justice Agnew in Brown v. Vandergrift, 80 Pac. St. 147, 148. They belong to the owner of the land and are part of it, so long as they are on or in it, and are subject to his control; but when they escape and go into other land, or come under another's control, the title of the former owner is gone. Possession of the land, therefore, is not necessarily possession of the gas. If an adjoining, or even a distant, owner drills his own land, and taps your gas, so that it comes into his well and under his control, it is no longer yours, but his."

Ohio, shortly thereafter, added its bit to this weird conception of ownership, and said of the Rule of Capture:

> "Whatever gets into the well belongs to the owner of the well, no matter where it came from. In such cases the well and its contents belong to the owner or lessee of the land, and no one can tell to a certainty from whence the oil, gas or water which enters the well came, and no legal right as to the same can be established or enforced by an adjoining land-owner."[7]

Concerning the offset rule, the same court added:

> "While it is generally supposed that oil is drained into wells for a distance of several hundred feet, the matter is somewhat uncertain, and no right of sufficient weight can be grounded upon such uncertain supposition to overcome the well-known right which every man has to use his property as he pleases, so long as he does not interfere with the legal rights of others. Protection of lines of adjoining lands by the drilling of wells on both sides of such lines affords an ample and sufficient remedy for the supposed grievances complained of in the petition and supplemental petition, without resort to either an injunction or an accounting."[8]

The summation of the idea was proclaimed in *Bernard v. Monongahela Gas Co.*,[9] which established the legal standard of co-operation among

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[7]Kelly v. Ohio Oil Co., 57 Ohio St. 317, 49 N.E. 399, 401, 39 A. L. R. 765, 768 (1897).

[8]*Ibid.*

[9]216 Pa. 362, 65 Atl. 801, 802 (1907). The Court said: "An oil or gas well may draw its production from an indefinite distance and in time exhaust a large space. Exact knowledge on this subject is not at present attainable, but the vagrant character of the mineral and the porous sand rock in which it is found and through which it moves fully justify the general conclusion we have stated above and have led to its general adoption by practical operators. 'The right of every landowner to drill a well on his own land at whatever spot he may see fit' certainly must

sharers in a common reservoir. This case definitely removed from oil and gas protection against despoilation by others that had always been afforded to property.

It is quite conceivable how the courts, in the earlier days of the oil industry, with their meager technical knowledge, with the lack of knowledge on the part of the operators as to the cause of the migration of oil and gas, and in the light of their inability to control the same, could have held in that manner, and with such wording. The courts must have considered their decisions inadequate, but, in view of the lack of a better rule, had to apply the reasonings adduced. It is inconceivable, however, how a court in this day and age, in view of the developments that have taken place in the sciences of geology, geophysics, petroleum engineering and technology, as well as the developments in the manner and methods of drilling for and producing crude oil, could proclaim the same doctrine.

Dean Henry M. Bates, of the Michigan Law School, expressed his ideas thus:

> "The effect of early court decisions, based upon the erroneous theories heretofore referred to, was to make legal the pumping of all of the oil and gas possible from every man's well. Thus in the larger fields one producer might, and, in fact, often did, pump vast quantities of oil and gas underlying lands belonging to or controlled by other producers. *This, in itself, violates any sane theory of property rights.*"[10]

The Doctrine of Ownership in Place

Hardwicke, in his article on the Rule of Capture[11] defines the Ownership in Place Doctrine as follows:

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be conceded. If, then, the landowner drills on his land at such a spot as best subserves his purpose, what is the standing of the adjoining landowner whose oil or gas may be drained by his well? He certainly ought not to be allowed to stop his neighbor from developing his own farm. There is no certain way of ascertaining how much of the oil and gas that comes out of the well was when in situ under this farm and how much under that. What, then, has been held to be the law? It is this, as we understand it, every landowner or his lessee may locate his wells wherever he pleases, regardless of the interests of others. He may distribute them over the whole farm or locate them only on one part of it. He may crowd the adjoining farms so as to enable him to draw the oil and gas from them. What, then, can the neighbor do? Nothing; only go and do likewise. He must protect his own oil and gas. He knows it is wild and will run away if it finds an opening and it is his business to keep it at home. This may not be the best rule; but neither the legislature or our highest court has given us any better. No doubt many thousands of dollars have been expended 'in protecting lines' in oil and gas territory that would not have been expended if some rule had existed by which it could have been avoided. Injunction certainly is not the remedy."

[10] Transactions American Institute of Mining and Metallurgical Engineers (1935).

[11] (1935) 13 Tex. L. Rev. 391.

> "The antithesis of the rule of Capture is: The owner of a tract of land owns the oil and gas in place and, should minerals migrate to a neighbor's land and be produced from wells thereon, title would not vest in the neighbor, but, to the contrary, the migrating oil or gas, or at least an amount equal to that which migrated, could be recovered by the true owner."[12]

The Ownership in Place Doctrine has been adopted by ten of the oil producing states.[13] The contrary doctrine, most commonly called the Non-Ownership Rule, upon which the Rule of Capture and the Offset Drilling Rule have been based, has been adopted by seven of the oil producing states.[14] This Non-Ownership Doctrine sometimes has been referred to as the Exclusive Rights Doctrine, because of the fact that the landowner, or his lessee, has the "exclusive right" to drill for oil or gas on his property and retain what he finds. It is seen, therefore, that in some states a landowner owns the oil and gas beneath his land, while in others he owns but a right, an exclusive right, to reduce such oil and gas to possession.

However, as a practical operating problem, this differentiation makes little or no difference in swaying the courts in their decisions. The Rule of Capture has been applied in every state, regardless of whether such state has approved the Ownership in Place Doctrine or has adopted the Exclusive Rights Doctrine. The landowner has the right to drain oil and gas from the neighboring land, and to exhaust, if he can, the reservoir content through his own wells.

No good purpose can be served by going into the decisions and reasonings that the courts used in reaching this conclusion, because even if we were convinced that they were wrong, the decisions are fact, and have existed for such a length of time that they have become established rules of property and judicial precedents which the courts invoke under the doctrine of *stare decisis*. This much we know, however, that a rule of law which says that a landowner may produce freely and without restraint through wells on his land, which is based upon the assumption that he owns all of the oil and gas he can produce from those wells, regardless of whether or not he has drained his neighbor's land, and which says that the remedy of the neighbor, in order to fully protect himself, is to drill as many wells as he can, is a rule which approves and sanctions hasty development, disorderly operations and immeasurable waste, as well as the complete destruction of correlative and co-equal rights.

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[12](1935) 13 Tex. L. Rev. 391, 393.

[13]Arkansas, Kansas, Michigan, Mississippi, Montana, New Mexico, Ohio, Pennsylvania, Tennessee, Texas, and West Virginia.

[14]California, Illinois, Indiana, Kentucky, Louisiana, New York, and Oklahoma.

The major objectives of the oil industry should be the efficient extraction of oil and gas as and when needed and the equitable distribution of the minerals among the owners. It is impossible to accomplish these objectives under the Rule of Capture, which is economically inadvisable, mechanically impracticable, politically unwise, and legally unsound. The Offset Drilling Rule, which advises "protect yourself as best you can," is now outdated. The Ownership in Place doctrine has not been enforced in view of the two other rules. In East Texas, the operators, after almost destroying each other, finally became convinced of their errors. It obviously takes time, experience and education to find the best way; but an educational campaign is not the quickest remedy for waste. Unless prevented in advance, conditions obtaining in the East Texas field will be repeated elsewhere. The courts have held that before an event occurs it is within the power of the state to legislate against its happening.[15] Prevention is always the best cure for economic evils.

Human nature is not changing, and repetitions of such conditions can be avoided only by the restraining hand of the law. Courts, of necessity, base their decisions upon precedents. Attorneys are compelled to accept the law as they find it and make their own cases consistent with the law, even though such consistency does not at times exist. However, a change in the economic conditions of the oil business should produce a similar change in the law. Business and society are interested only in economic and social results. When the path of the law leads to absurd results and unsound economic conditions, state governments must function so as to straighten that path, and legislative enactment of proper laws is a vital necessity. The state has two powers, one to conserve the natural resources, and the other to protect the correlative right of the landowners. Science now offers means of production control far superior to the old methods. The law should keep pace.

How the law has endeavored to build itself up to keep pace with the advancement of science in the petroleum industry is the next consideration.

The Background of Conservation Legislation

In the beginning it is necessary to refer to certain principles that were firmly imbedded in the constitutional law of the country as a result of cases wherein the police power of the state met and opposed the due

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[15]Walls v. Midland Carbon Co., 254 U. S. 300, 41 Sup. Ct. 118, 65 L. ed. 276 (1920).

process clause of the Fourteenth Amendment to the Constitution of the United States. In determining the scope of police power, local conditions must be considered and taken into account.[16] The Supreme Court of the United States has attached considerable weight to decisions by the highest state courts in upholding legislation on the grounds that the public policy of such state demands a police measure of that particular type; and has said that unless such local legislation is manifestly unconstitutional, it will uphold the same.[17] A similar line of reasoning was employed by the Supreme Court in the recent case of *Railroad Commission of Texas v. Rowan & Nichols Oil Co.*,[18] where, in a four to three decision, Justice Frankfurter, speaking for the majority of the court, said:

> "But whether a system of proration based upon hourly potential is as fair as one based upon estimated recoverable reserves or some other factor or combination of factors, is in itself a question for administrative and not judicial judgments."[19]

And again:

> "Certainly in a domain of knowledge still shifting and growing and in a field where judgment is therefore necessarily beset by the necessity of inferences bordering on conjectures even for those learned in the art, it would be presumption for courts, on the basis of conflicting expert testimony, to deem the view of the administrative tribunal, acting under legislative authority, offensive to the Fourteenth Amendment."[20]

And concluded:

> "It is not for the federal courts to supplant the Commission's judgment even in the face of convincing proof that a different result would have been better."[21]

It is well recognized that the scope of police power depends upon conditions as they may change from time to time; and that a measure which would have been held invalid in a state of society or under eco-

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[16]Terrace v. Thompson, 263 U. S. 197, 44 Sup. Ct. 15, 68 L. ed. 255 (1923); Bacon v. Walker, 204 U. S. 311, 27 Sup. Ct. 289, 51 L. ed. 499 (1907).

[17]Gant v. Oklahoma City, 289 U. S. 98, 53 Sup. Ct. 530, 77 L. ed. 1058 (1933); Sproles v. Burford, 286 U. S. 374, 52 Sup. Ct. 581, 76 L. ed. 1167 (1932); Gorieb v. Fox, 274 U. S. 603, 47 Sup. Ct. 675, 71 L. ed. 1228 (1927); Zahn v. Board of Public Works, 274 U. S. 325, 47 Sup. Ct. 594, 71 L. ed. 1074 (1927); Levy v. Siegel, 258 U. S. 242, 42 Sup. Ct. 289, 66 L. ed. 595 (1922). For rather extreme views on this subject see Nebbia v. New York, 291 U. S. 502, 54 Sup. Ct. 505, 78 L. ed. 940 (1940); and Miller v. Schoene, 276 U. S. 272, 48 Sup. Ct. 246, 72 L. ed. 568 (1928).

[18]310 U. S. 573, 60 Sup. Ct. 1021, 84 L. ed. 1368 (1940).

[19]*Id.* at 581, 60 Sup. Ct. at 1024, 84 L. ed. at 1373.

[20]*Ibid.*

[21]*Id.* at 584, 60 Sup. Ct. at 1025, 84 L. ed. at 1374.

nomic conditions previously existing, might be held constitutional by reason of a change in circumstances or conditions.[22] In delving into the history of the various oil conservation statutes of the several states, it must be borne in mind that the legislatures, in formulating measures for the benefit of the social and economic welfare of the people of the state, do not view the legislation as to immediate appearance or effect. In enactments of this nature, the legislatures naturally look as far into the future as possible.[23] Then, again, it may be stated that where an act of a state legislature, passed under the police power of the state, is debatable in relation to the due process clause of the Fourteenth Amendment, the act will be upheld.[24]

If mere localization is a circumstance which, under our system, must be considered in determining the validity of a state statute enacted to promote the betterment of the people, then no other business or enterprise possesses the quality of locality more than does the oil business. While a number of the states produce oil in small quantities, the chief dependence of the country at the present time for petroleum reserves is upon the supply found in about eight states.[25] It is in these few states that the necessity for regulating the business of producing oil so as to control the reservoir energy for larger ultimate recovery is greatest. This observation is so, whether the purpose of the measure is to conserve for the needs of the state, or to adjust the correlative rights of the oil operators interested in the same pool.

The fact remains, however, that in no oil state is the public opinion of the oil industry the controlling factor in bringing about the enactment of measures regulating the business. It is admitted that the men in the industry and their experience, training, and skill, have an important effect upon the nature of the regulations enacted. At the same time, however, the force exerting the most influence and perserverance in attempting to establish oil control emanates from the state itself, and not from the industry.

It is trite to say that in testing a police statute against the "due process" clause of the Constitution, the public welfare of the community,

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[22]Village of Euclid v. Ambler Realty Co., 272 U. S. 365, 47 Sup. Ct. 114, 71 L. ed. 303 (1926); Block v. Hirsh, 256 U. S. 135, 41 Sup. Ct. 458, 65 L. ed. 865 (1921).

[23]Zahn v. Board of Public Works, 274 U. S. 325, 47 Sup. Ct. 594, 71 L. ed. 1074 (1927); Village of Euclid v. Ambler Realty Co., 272 U. S. 365, 47 Sup. Ct. 114, 71 L. ed. 303 (1926).

[24]See cases cited *supra* note 17.

[25]Texas, California, Oklahoma, Illinois, Louisiana, Kansas, New Mexico, and Arkansas.

the people and the state, is always the most important factor, and usually the controlling factor in the case. Fundamentally, private rights must yield to police power because the general welfare of the state so commands. The immunity of property rights under constitutional guaranties from the constantly expanding police powers of the state is not a simple question, and no court ever has laid down a specific and final rule which unerringly will draw the line between the two concepts. It is well settled that each case must be considered and determined upon its particular facts. The cases thereon are so numerous and well known that it is unnecessary to refer to them. However, there are broad holdings of the Supreme Court of the United States that should be of value. It is both an economic and legal principle that the highest attribute of property is the right of the owner to use and enjoy the subject thereof according to its peculiar nature and adaptiveness.[26] The courts today ascribe the broadest possible operation to the police power of the states.[27] Because of the fact that the local legislature and the court of a state are familiar with the needs of that particular jurisdiction, their determination that the public policy of such state demands a police measure of a particular type will have great weight with the Supreme Court if it is called upon to determine the constitutionality of that measure.[28] Mr. Justice Holmes, in the case of *Pennsylvania Coal Co. v. Mahon,*[29] said, in effect, that the decision of any question involving

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[26]Pennsylvania Coal Co. v. Mahon, 260 U. S. 393, 43 Sup. Ct. 158, 67 L. ed. 322 (1922); Buchanan v. Warley, 245 U. S. 60, 38 Sup. Ct. 16, 62 L. ed. 149 (1917).

[27]It may be said in a general way that police power not only includes regulations to promote the health, peace, morals and good order of the people, but also the power to legislate so as to increase the industries of the state, develop its resources, and add to its wealth and prosperity. Barbier v. Connolly, 113 U. S. 27, 5 Sup. Ct. 357, 28 L. ed. 923 (1885).

"We hold that the police power of the state embraces regulations designed to promote public convenience or the general prosperity as well as regulations to promote the public health, the public morals or the public safety." Chicago, B. & Q. Ry. v. Illinois, 200 U. S. 561, 592, 26 Sup. Ct. 341, 50 L. ed. 596, 609, (1906).

The power of the state to prevent unnecessary loss, destruction or waste in the reduction of oil and gas to the possession of owners of the overlying land extends to the prevention of unreasonable and wasteful use of natural gas pressure available for lifting the oil to the surface and the unreasonable and wasteful depletion of the common source of supply to the injury of others entitled to take from the same pool. Champlin Refining Co. v. Corp. Comm. of Okla., 286 U. S. 210, 52 Sup. Ct. 559, 76 L. ed. 1062 (1932). See also Zahn v. Board of Public Works, 274 U. S. 325, 47 Sup. Ct. 594, 71 L. ed. 1074 (1927); Village of Euclid v. Ambler Realty Co., 272 U. S. 365, 47 Sup. Ct. 114, 71 L. ed. 303 (1926); Block v. Hirsh, 256 U. S. 135, 41 Sup. Ct. 458, 65 L. ed. 865 (1921); The Slaughter House Cases, 16 Wall. 36, 21 L. ed. 394 (U. S. 1873).

[28]If the question between the taking of property and a proper exercise of police power is fairly debatable, the statute will be upheld. Gorieb v. Fox, 274 U. S. 603, 47 Sup. Ct. 675, 71 L. ed. 1228 (1927); Weaver v. Palmer Bros., 270 U. S. 402, 46 Sup. Ct. 320, 70 L. ed. 654 (1926); Noble State Bank v. Haskell, 219 U. S. 104, 31 Sup. Ct. 186, 55 L. ed. 112 (1911); Muller v. Oregon, 208 U. S. 412, 28 Sup. Ct. 324, 52 L. ed. 551 (1908).

[29]260 U. S. 393, 43 Sup. Ct. 158, 67 L. ed. 322 (1922), cited *supra* note 26.

the constitutional guaranties on one side and the exercise of police powers on the other, depends upon the degree of diminution that is brought about by the police measure, which is another way of saying that the case depends upon whether or not the statute goes too far.

The State's power to legislate for the protection of its natural resources, whether under one or the other of the theories hereinafter advanced, is based essentially upon its police power. Certain constitutional checks have been urged against the exercise of such police power, the most important ones being (a) deprivation of property without due process of law;[30] (b) denial of equal protection of the laws;[31] (c) impairment of the obligations of a contract;[32] (d) interference with interstate commerce.[33] Other, and minor checks have been (a) delegation of

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[30]Champlin Refining Co. v. Corp. Comm. of Okla., 286 U. S. 210, 52 Sup. Ct. 559, 76 L. ed. 1062 (1932); Sterling v. Constantin, 287 U. S. 378, 53 Sup. Ct. 190, 77 L. ed. 375 (1932); Lindsley v. Natural Carbonic Gas Co., 220 U. S. 61, 31 Sup. Ct. 337, 55 L. ed. 369 (1911); Ohio Oil Co. v. Indiana, 177 U. S. 190, 20 Sup. Ct. 576, 77 L. ed. 729 (1900); Texoma Natural Gas Co. v. R. R. Comm. 59 F.(2d) 750 (W. D. Tex. 1932); McMillan v. R. R. Comm. of Tex., 51 F.(2d) 400 (W. D. Tex, 1931); Oxford Oil Co. v. Atlantic Oil & Producing Co., 16 F.(2d) 639 (N. D. Tex. 1926), *aff'd*, 22 F.(2d) 597 (C.C.A. 5th, 1927); Given v. State, 160 Ind. 552, 66 N.E. 750 (1903); Townsend v. State, 147 Ind. 624, 47 N.E. 19, 37 L. R. A. 294 (1897); Gas Products Co. v. Rankin, 63 Mont. 372, 207 Pac. 993, 24 A. L. R. 294 (1924); H. F. Wilcox Oil & Gas Co. v. State, 162 Okla. 89, 19 P.(2d) 374 (1932); Russell v. Walker, 15 P.(2d) 114 (Okla. 1932); Julian Oil & Royalties Co. v. Capshaw, 147 Okla. 237, 292 Pac. 841 (1930); Danciger Oil & Refining Co. v. R. R. Comm. of Tex., 49 S.W.(2d) 837 (Tex. 1932).

[31]Champlin Refining Co. v. Corp. Comm. of Okla., 286 U. S. 210, 52 Sup. Ct. 559, 76 L. ed. 1062 (1932); Bandini Petroleum Co. v. Superior Court, 284 U. S. 8, 52 Sup. Ct. 103, 76 L. ed. 136 (1931); Walls v. Midland Carbon Co., 254 U. S. 300, 41 Sup. Ct. 118, 65 L. ed. 276 (1920); Lindsley v. Natural Carbonic Gas Co., 220 U. S. 61, 31 Sup. Ct. 337, 55 L. ed. 369 (1911); People v. Associated Oil Co., 211 Cal. 93, 294 Pac. 717 (1930), *aff'd*, 212 Cal. 76, 296 Pac. 536 (1931); Danciger Oil & Refining Co. v. R. R. Comm. of Tex., 49 S.W.(2d) 837 (Tex. 1932).

[32]Walls v. Midland Carbon Co., 254 U. S. 300, 41 Sup. Ct. 118, 65 L. ed. 276 (1920); Producers Transportation Co., v. Railroad Commission, 251 U. S. 228, 49 Sup. Ct. 121, 64 L. ed. 239 (1920); Texoma Natural Gas Co. v. R. R. Comm. of Tex., 59 F.(2d) 750 (W. D. Tex. 1932); Oxford Oil Co. v. Atlantic Oil & Producing Co., 16 F.(2d) 639 (N. D. Tex. 1926), *aff'd*, 22 F.(2d) 597 (C.C.A. 5th, 1927).

[33]Champlin Refining Co. v. Corp. Comm. of Okla., 286 U. S. 210, 52 Sup. Ct. 559, 76 L. ed. 1062 (1932); Pennsylvania v. West Virginia, 262 U. S. 553, 43 Sup. Ct. 658, 67 L. ed. 117 (1923); Haskell v. Kansas Natural Gas Co., 224 U. S. 217, 32 Sup. Ct. 442, 56 L. ed. 738 (1912); Lindsley v. Natural Carbonic Co., 220 U. S. 61, 31 Sup. Ct. 337, 55 L. ed. 369 (1911); West v. Kansas Natural Gas Co., 221 U. S. 229, 31 Sup. Ct. 564, 55 L. ed. 716 (1911); Texoma Natural Gas Co. v. R. R. Comm. of Tex., 59 F.(2d) 750 (W. D. Tex. 1932); McMillian v. R. R. Comm. of Tex., 51 F.(2d) 400 (W. D. Tex. 1932); Manufacturers Gas & Oil Co. v. Indiana Natural Gas Co., 156 Ind. 679, 59 N.E. 169 (1901), *pet'n for rehearing overr.*, 156 Ind. 679, 60 N.E. 1080 (1901); Manufacturers Oil & Gas Co. v. Indiana Natural Gas Co., 155 Ind. 566, 58 N.E. 851 (1900); Manufacturers Gas & Oil Co. v. Indiana Natural Gas Co., 155 Ind. 545, 58 N.E. 706 (1900); Manufacturers Gas & Oil Co. v. Indiana Natural Gas Co., 155 Ind. 461, 57 N.E. 912, 50 L. R. A. 768 (1900); State *ex rel* Corwin v. Indiana & Ohio Oil & Gas Co., 120 Ind. 575, 22 N.E. 778 (1899); Consumers Gas Trust Co. v. Harless, 131 Ind. 446, 29

legislative authority to administrative bodies;[34] and (b) price fixing characteristics.[35] Mr. Justice Holmes, in *Hudson County Water Co. v. McCarter*,[36] ably defined the "limits" of police power in saying:

> "All rights tend to declare themselves absolute to their logical extreme. Yet all in fact are limited by the neighborhood of principles of policy which are other than those on which the particular right is founded, and which becomes strong enough to hold their own when a certain point is reached. The limits set to property by other public interests present themselves as a branch of what is called the police power of the State. The boundary at which the conflicting interests balance can not be determined by any general formula in advance, but points in the line, or helping to establish it, are fixed by decisions that this or that concrete case falls on the nearer or farther side. For instance, the police power may limit the height of buildings in a city without compensation. To that extent it cuts down what otherwise would be the rights of property. But if it should attempt to limit the height so far as to make an ordinary building lot wholly useless, the rights of property would prevail over the other public interest, and the police would need the compensation and the power of eminent domain."

The cases hereinbefore quoted[37] represent the "limits" urged against conservation legislation. The cases, all in all, indicate that the courts overwhelmingly recognize the responsibility, power and authority of the state to enact such legislation.

N.E. 1062, 15 L. R. A. 505 (1892); Jamieson v. Indiana Natural Gas & Oil Co., 128 Ind. 555, 28 N.E. 76 (1891); Benedict v. Columbus Construction Co., 49 N. J. Eq. 33, 23 Atl. 485 (1892); Russell v. Walker, 15 P.(2d) 115 (Okla. 1932); Julian Oil & Royalties Co. v. Capshaw, 147 Okla. 237, 292 Pac. 841 (1930); Sneed v. Tippett, 114 Okla. 173, 245 Pac. 40 (1925); Danciger Oil & Refining Co. v. R. R. Comm. of Tex., 49 S.W.(2d) 837 (Tex. 1932).

[34]Champlin Refining Co. v. Corp. Comm. of Okla., 286 U. S. 210, 52 Sup. Ct. 559, 76 L. ed. 1062 (1932); Bandini Petroleum Co. v. Superior Court, 284 U. S. 8, 52 Sup. Ct. 103, 76 L. ed. 136 (1931); Oxford Oil Co. v. Atlantic Oil & Producing Co., 16 F.(2d) 639 (N. D. Tex., 1926), *aff'd*, 22 F.(2d) 597 (C.C.A. 5th, 1927); People v. Associated Oil Co., 211 Cal. 93, 294 Pac. 717 (1930), *aff'd*, 212 Cal. 76, 296 Pac. 536 (1931); Julian Oil & Royalties Co. v. Capshaw, 147 Okla. 237, 292 Pac. 841 (1930); Quinton Relief Oil & Gas Co. v. Corp. Comm. of Okla., 101 Okla. 164, 224 Pac. 156 (1924); Danciger Oil & Refining Co. v. R. R. Comm. of Tex., 49 S.W.(2d) 837 (Tex. 1932); Peterson v. Grayce Oil Co., 37 S.W.(2d) 367 (Tex. 1931).

[35]Champlin Refining Co. v. Corp. Comm. of Okla., 286 U. S. 210, 52 Sup. Ct. 559, 76 L. ed. 1062 (1932); People v. Associated Oil Co., 211 Cal. 93, 294 Pac. 717 (1930) *aff'd*, 212 Cal. 76, 296 Pac. 536 (1931); Julian Oil & Royalties Co. v. Capshaw, 147 Okla. 237, 292 Pac. 841 (1930).

[36]209 U. S. 349, 355, 28 Sup. Ct. 529, 52 L. ed. 828, 832 (1908).

[37]See cases cited *supra* notes 30-36 inclusive.

The Theories Supporting a State's Power to Enact Conservation Legislation

A review of the cases involving the constitutionality of conservation legislation has established the existence of two fundamental theories upon which the state may regulate the extraction of oil and gas. First, the state, by virtue of its interest in the protection of its natural resources, may legislate to insure against waste.[38] Second, the state, to insure ratable taking from a common reservoir or pool, may legislate to regulate the correlative rights of the common owners of the pool.[39] A third, and

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[38]*California:* Bandini Petroleum Co. v. Superior Court, 284 U. S. 8, 52 Sup. Ct. 103, 76 L. ed. 136 (1931); People v. Associated Oil Co., 211 Cal. 23, 294 Pac. 717 (1930), *aff'd,* 212 Cal. 76, 296 Pac. 536 (1931). *Indiana:* Ohio Oil Co. v. Indiana, 177 U. S. 190, 20 Sup. Ct. 576, 44 L. ed. 729 (1900); State v. Alleghany Oil Co., 85 Fed. 870 (C. C. D. Ind. 1898); Bailey v State, 163 Ind. 165, 71 N.E. 655 (1904); State v. Ohio Oil Co., 150 Ind. 21, 49 N.E. 809, 47 L. R. A. 627 (1898). *Kansas:* Marrs v. City of Oxford, 24 F.(2d) 541 (D. Kan. 1928), *aff'd,* 32 F.(2d) 134 (C.C.A. 8th, 1929); Helmerick & Payne v. Roxana Petroleum Corp., 136 Kan. 254, 14 P.(2d) 663 (1934). *Kentucky:* Commonwealth v. Trent, 117 Ky. 34, 77 S.W. 390 (1903). *Louisiana:* Harkness v. Irion, 11 F.(2d) 386 (E. D. La. 1926); State v. Thrift Oil & Gas Co., 162 La. 165, 110 So. 188 (1926). *Missouri:* Myron Green Cafeteria v. Kansas City, 203 Mo. 519, 240 S.W. 132 (1922). *Montana:* Gas Products Co. v. Rankin, 63 Mont. 372, 207 Pac. 993, 24 A. L. R. 294 (1924). *New Mexico:* Eccles v. Ditto, 167 Pac. 126, L. R. A. 1918B 126 (N. M. 1917). *New York:* Hathorn v. Natural Carbonic Gas Co., 194 N. Y. 326, 87 N.E. 504 (1909). *Oklahoma:* Champlin Refining Co. v. Corp. Comm. of Okla. 286 U. S. 210, 52 Sup. Ct. 559, 76 L. ed. 1062 (1932); Russell v. Walker, 15 P.(2d) 114 (Okla. 1932); Julian Oil & Royalty Co. v. Capshaw, 147 Okla. 237, 292 Pac. 841 (1930); Anderson Kerr v. Van Meter, 162 Okla. 176, 19 P.(2d) 1068 (1932); Quinton Relief Oil & Gas Co. v. Corp. Comm. of Okla., 101 Okla. 164, 224 Pac. 156 (1924). *Pennsylvania:* Hague v. Wheeler, 157 Pa. St. 324. *Texas:* Sterling v. Constantin, 287 U. S. 378, 53 Sup. Ct. 190, 77 L. ed. 375 (1932); Constantin v. Smith, 57 F.(2d) 227 (E. D. Tex. 1932); Henderson v. R. R. Comm. of Tex., 56 F.(2d) 218 (W. D. Tex. 1932); Oxford Oil Co. v. Atlantic Oil & Producing Co., 16 F.(2d) 639 (M. D. Tex. 1926), *aff'd,* 22 F.(2d) 597 (C.C.A. 5th, 1927); Danciger Oil & Refining Co. v. R. R. Comm. of Tex., 49 S.W.(2d) 837 (Tex. 1932); Humble Oil & Refining Co. v. Strauss, 243 S.W. 528 (Tex. 1922). *Wyoming:* Walls v. Midland Carbon Co., 254 U. S. 300, 41 Sup. Ct. 118, 65 L. ed. 276 (1920).

[39]*California:* Bandini Petroleum Co. v. Superior Court, 284 U. S. 8, 52 Sup. Ct. 103, 76 L. ed. 136 (1931); People v. Associated Oil Co., 211 Cal. 23, 294 Pac. 717 (1930) *aff'd,* 212 Cal. 76, 296 Pac. 536 (1931); Ex Parte Elam, 6 Cal. App. 233, 91 Pac. 811 (1907). *Indiana:* Ohio Oil Co. v. Indiana, 177 U. S. 190, 20 Sup. Ct. 576, 44 L. ed. 729 (1900); Manufacturers Gas & Oil Co. v. Indiana Natural Gas Co., 156 Ind. 679, 59 N.E. 169 (1901), *pet'n for rehearing overr.,* 156 Ind. 679, 60 N.E. 1080 (1901); Manufacturers Oil & Gas Co. v. Indiana Natural Gas Co., 155 Ind. 566, 58 N.E. 851 (1900); Manufacturers Gas & Oil Co. v. Indiana Natural Gas Co., 155 Ind. 545, 58 N.E. 706 (1900); Manufacturers Gas & Oil Co. v. Indiana Natural Gas Co., 155 Ind. 461, 57 N.E. 912, 50 L. R. A. 768 (1900); Townsend v. State, 147 Ind. 624, 47 N.E. 19, 37 L. R. A. 294 (1897). *Kansas:* Marrs v. City of Oxford, 24 F.(2d) 541 (D. Kan. 1928), *aff'd,* 32 F.(2d) 134 (C.C.A. 8th, 1929); Arnold v. Garnett Light & Fuel Co., 103 Kan. 477, 174 Pac. 1027 (1918). *Kentucky:* Louisville Gas Co. v. Kentucky Heating Co., 117 Ky. 71, 77 S.W. 368, 70 L. R. A. 558 (1903). *Louisiana:* Louisiana Gas & Fuel Co. v. White Bros., 157 La. 728, 103 So. 23 (1925); Higgins Oil & Fuel Co. v. Guaranty Oil Co., 145 La. 233, 82 So. 206, 5 A. L. R. 411 (1919); *New York:* Lindsley v. Natural Carbonic Gas Co., 220 U. S. 61, 31 Sup. Ct. 337, 55 L. ed. 369 (1911); People v.

somewhat minor theory, is that the state may abate as a nuisance operations which tend to endanger life or property.[40]

The Police Power of the State, Exercised in the Public Interest, as a Basis for the Constitutionality of Conservation Statutes

There is a penetrating and deeply rooted public interest which for three reasons must impel any oil producing state to bring about conditions that will result in the longest possible life to the oil fields in that state, with the largest ultimate recovery from such fields. The first of these reasons is that the state, as owner, holds title to a considerable amount of acreage, either in school lands, water bottoms, or, in the case of coastal states, in the bottom of the ocean beyond the shores. In most of the states some of these lands have already been developed; and, if exploration for oil on the scale that it is now being conducted continues, oil production should be found on other tracts of land belonging to the state. The bonuses and royalties from leasing, development and production accordingly go into the various funds set up by the states to receive them.

The second reason, which involves a public interest phase that is of even greater importance, is the fact that the oil and gas industry of

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New York Carbonic Gas Co., 196 N. Y. 421, 90 N.E. 441 (1909); Hathorn v. Natural Carbonic Gas Co., 194 N. Y. 326, 87 N.E. 504 (1909). *Oklahoma:* Patterson v. Stanolind Oil & Gas Co., 305 U. S. 376, 59 Sup. Ct. 259, 83 L. ed. 231 (1938); Champlin Refining Co. v. Corp. Comm. of Okla., 286 U. S. 210, 52 Sup. Ct. 559, 76 L. ed. 1062 (1932); Wilcox Oil & Gas Co. v. Walker, 168 Okla. 355, 32 P.(2d) 1044 (1934); Russell v. Walker, 15 P.(2d) 115 (Okla. 1932); Julian Oil & Royalty Co. v. Capshaw, 145 Okla. 237, 292 Pac. 841 (1930); *Texas:* Oxford Oil Co. v. Atlantic Oil & Producing Co., 16 F.(2d) 639 (N. D. Tex. 1926), *aff'd*, 22 F.(2d) 597 (C.C.A. 5th, 1927); Peterson v. Grayce Oil Co., 37 S.W.(2d) 367 (Tex. 1931). *Wyoming:* Walls v. Midland Carbon Co., 254 U. S. 300, 41 Sup. Ct. 118, 65 L. ed. 276 (1920).

[40] *Indiana:* Given v. State, 160 Ind. 552, 66 N.E. 750 (1903); State v. Ohio Oil Co., 150 Ind. 21, 49 N.E. 809, 47 L. R. A. 627 (1898); Tyner v. Peoples Gas Co., 131 Ind. 408, 31 N.E. 61 (1892); Peoples Gas Co. v. Tyner, 131 Ind. 277, 31 N.E. 59 (1892); Jamieson v. Indiana Natural Gas & Oil Co., 128 Ind. 555, 28 N.E. 76 (1891). *Kansas:* State v. Lebow, 128 Kan. 715, 280 Pac. 773 (1929); Winkler v. Anderson, 104 Kan. 1, 177 Pac. 521, 3 A. L. R. 268 (1919). *Kentucky:* Palmer Corp. v. Collins, 214 Ky. 838, 284 S.W. 95 (1926). *Louisiana:* Louisiana Gas & Fuel Co. v. White Bros. 157 La. 728, 103 So. 23 (1925); Higgins Oil & Fuel Co. v. Guaranty Oil Co., 145 La. 233, 82 So. 206, 5 A. L. R. 411 (1919). *New Mexico:* Eccles v. Ditto, 167 Pac. 126, L. R. A. 1918B 126 (N. M. 1917). *Oklahoma:* Verland Oil & Gas Co. v. Walker, 100 Okla. 258, 229 Pac. 235 (1924); Gulf Pipeline Co. v. Pawnee Petrol Co., 34 Okla. 775, 127 Pac. 252, 41 L. R. A. (N.S.) 1108 (1912). *Ohio:* Cline v. Kirbride, 22 Ohio C. C. 527 (1901). *Pennsylvania:* Steelsmith v. Aiken, 14 Pa. Super. 226 (1900). *Texas:* R. R. Comm. of Tex. v. Bass, 10 S.W.(2d) 587 (1928); Texas Pacific Coal & Oil Co. v. Comanche Duke Oil Co., 274 S.W. 193 (Tex. 1925), *rev'd* 298 S.W. 554 (Tex. 1927). *West Virginia:* Atkinson v. Virginia Oil & Gas Co., 72 W. Va. 707, 79 S.E. 647 (1913); Tabott v. Southern Oil Co., 60 W. Va. 423, 55 S.E. 1009 (1907); McGregor v. Camden, 47 W. Va. 193, 34 S.E. 274 (1899).

the various states that have been developed to a considerable extent is on of the major revenue producing industries in such states. It is an item of common knowledge that if Oklahoma, Louisiana, Texas, and the other producing states were considered economically without regard to the oil industry, such states would be strictly agricultural. There would be some mining, of salt and sulphur in the Gulf Coast States, and possibly coal and other minerals to a small extent in the inland areas. There would also be lumbering; but none of these industries contributes to the prosperity of the state as does the oil industry. The economic structure of such states is built on agriculture, plus some factories and mining, and the oil industry. Examination of employment in the oil industry reveals the following classification; (a) The field and office workers of the oil companies; (b) the field and office workers of the pipeline companies; (c) the field and office workers of the refineries; (d) the field and and office workers of the supply houses; (e) the workers of the manufacturers of oil equipment that are in the state; (f) the trucking industry employees that are brought into the state for the petroleum industry alone; (g) the geological and geophysical branch of the industry, that brings men and equipment into the state; (h) the employees of the independent contractors that gather around oil fields; (i) lease brokers and dealers.

Practically every grant under which oil is sought and from which it is produced is by a farmer. Out of these leases the farmer receives bonuses, rentals and royalties. In every important oil-producing state, save Illinois, which is new to the industry, and Mississippi, which cannot yet be classified as an important oil-producing state, the oil industry directly hires more employees than any other enterprise or business in the state. Indirectly, too, the industry gives employment to many, many thousands more. The bonuses, rentals and royalties paid, the wages of those employed in the oil industry, either directly or indirectly, find their way into every channel of commerce and industry in the state. In all but one[41] of important oil producing states a large part of the state's revenue comes from the imposition of production and severance taxes upon the oil industry.[42] In other ways taxable wealth of many other kinds, directly attached to the oil industry, is brought into the state and composes a source of revenue to which the state and its political subdivisions may, and do, resort.

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[41]California.

[42]*Arkansas:* ARK. DIG. STAT. (Pope, 1937) §§ 13374, 13376, 13378-95. *Louisiana:* LA. GEN. STAT. ANN. (Dart, 1939) §§ 8522, 8543. *New Mexico:* N. M. STAT. ANN. (Courtright, 1929) §§ 97-401, 97-406. *Oklahoma:* OKLA. STAT. (Harlow, 1931) § 12428-9. *Texas:* TEX. STAT. (Vernon, 1936) Art. 6032-32a.

It is obvious, then, that the merchant, the banker, the lawyer, the doctor, the farmer, the worker, and all who are interested in the general welfare of the state, prosper by reason of the oil industry; and the necessity for every one of the oil-producing states to do all within its power to bring into and retain in the state the industry that means sc much to it is correspondingly obvious. This retention is best had by prolonging the life of the fields in which the companies operate. The productive life of the fields is best maintained by adequate and proper conservation laws, even though such laws may and have been subject to attack as being unconstitutional as an undue extension of the police powers of the state and violative of the due process clause of the Fourteenth Amendment. It has become a matter of state public policy to foster and encourage the business of producing oil and to furnish it with the technology so important in prolonging the productive life of the industry for as long a period as possible. In *Julean Oil & Royalties Co. v. Capshaw*[43] this was referred to as being legitimate grounds for the upholding of a regulation of the producing branch of the oil industry.

But it must be realized that while the revenue producing possibilities of the oil and gas industry are of considerable importance and cannot be disregarded when public interest and private rights are compared with it, as must be done when due process is invoked, there is involved the third important element of public interest. This third and most important reason is so axiomatic and well known, that it need hardly be touched upon herein. Suffice it to say that this reason is the deep-seated interest of the state and the public in general in the preservation of the natural resources of the country, and in their judicious use. This reason is all-inclusive and embraces the interest of the state in public-owned land, because of the revenue derived therefrom, the interest of the public in the industry, as in an oil producing industry, and the interest of both in the conservation of such resources and their protection against waste. They go hand in hand. It has often been stated, and it cannot be denied, that in the past the American people have been notorious in their deliberate, intentional and indifferent exploitation of the natural resources of their great country, especially their minerals and timber. This indifference came into being despite the fact that the present generation of Americans, following the precepts of generations gone by, often has voiced the principle that one should not waste or impair his inherited patrimony. Now the preservation of our natural resources most assuredly finds the approval of the vast majority of the citizens

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[43]145 Okla. 237, 292 Pac. 841 (1930).

of the country. The people are now becoming educated to the fact that our resources must be conserved and preserved. They favor conservation statutes.

Therefore, in considering the important point of police power, based upon public interest, public welfare and good, as against due process of law, it is shown that the state, as an entity, because of revenue derived, general prosperity and public interest, has a tremendous interest in prolonging the life of an oil field, and in seeing that the recovery therefrom is as great as possible. Matters of supreme public welfare and public interest are involved, as against private operations based upon the Fourteenth Amendment.

The Supreme Court has defined police power as including, not only the power to make regulations to promote the health, peace, morals and good order of the people, but also the power to legislate so as to increase the industries of the state, develop its resources, and add to its wealth and prosperity.[44] Consequently when an industry enters into the economic and fiscal structure of a state in the manner and to the extent that the oil industry does, regulations in so far as they affect the life of the fields operated by such industry clearly should be within the principles enunciated.

The Correlative Rights Doctrine as a Basis for the Constitutionality of Conservation Statutes

Forty years ago the United States Supreme Court handed down a momentous and historic decision in *Ohio Oil Co. v. Indiana.*[45] The case involved the constitutionality of a statute enacted for the prevention of waste of gas through its escape from oil wells. The decision held that the power to enact such a measure existed in the legislature and could "be manifested for the purpose of protecting all the collective owners [of land in a petroleum reservoir] by securing a just distribution to arise from the enjoyment by them of their privilege to reduce to possession. . . ." It was further held that the state may grant protection to collective landowners in a petroleum reservoir, each against the injurious conduct on the part of the others to the reservoir, and that the protection which the state may grant is to secure *just distribution* of the oil and gas contained in the common reservoir.

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[44]Barbier v. Connolly, 113 U. S. 27, 5 Sup. Ct. 357, 28 L. ed. 923 (1885), cited *supra* note 27. See also Nebbia v. New York, 291 U. S. 502, 54 Sup. Ct. 505, 78 L. ed. 940 (1934); Miller v. Schoene, 276 U. S. 272, 48 Sup. Ct. 246, 72 L. ed. 568 (1928.)

[45]Ohio Oil Co. v. Indiana, 177 U. S. 190, 20 Sup. Ct. 576, 44 L. ed. 729 (1900); State v. Ohio Oil Co., 150 Ind. 21, 49 N.E. 809 (1898).

It must be borne in mind that this decision upheld the constitutionality of a statute *abridging* the right of an operator to produce as freely as he would like. This decision was the first in which the courts began to give recognition to the physical properties of oil and gas, and the method of production. The Rule of Capture was discussed and the fallacies of the comparison of oil and gas to animals *ferae naturae* were pointed out. While it was true that title to the land carried with it the right to the minerals beneath the surface, and the right to mine for such minerals, there was another right involved—the co-equal right of all the owners of the reservoir to take from the common source of supply. The owners of the land covering a reservoir of oil, a common source of supply, are entitled to share equitably in the contents of such reservoir. The taking by one owner of a share greater than the other would result in "an undue proportion being attributed to one of the possessors of the right, to the detriment of others, or by waste by one or more, to the annihilation of the rights of the remainder."[46] Thus was originated the doctrine of correlative rights, by the highest tribunal of justice in the land. The true meaning of this doctrine is that the rights of one owner in a common reservoir of oil are limited by his duty to the other owners not to injure the reservoir, nor to take more than a just portion of the oil or gas found therein, nor to commit waste in the production thereof. From these considerations the Court came to the conclusion that states have the power to protect the co-equal and correlative rights of landowners by the enactment of proper legislation designed to secure a just distribution of recovery from the common reservoir, and said "there must arise the legislative power to protect the rights of property from destruction." That this doctrine is applicable not only to the "ownership in place" states, but also to the "exclusive right" states, is readily seen from the following statement of the Court:

> "If the right of the collective owners of the surface to take from the common fund, and thus reduce a portion of it to possession, does not create a property interest in the common fund, then the statute does not provide for the taking of private property without compensation. If, on the other hand, there be, as a consequence of the right of the surface owners to reduce to possession, a right of property in them in and to the substances contained in the common reservoir of supply, then, as a necessary result of the right of property, its indivisible quality, and the peculiar position of the things to which it relates, there must arise the legislative power to protect the right of property from destruction. To illustrate by another

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[46]Ohio Oil Co. v. Indiana, 177 U. S. 190, 210, 20 Sup. Ct. 576, 584, 44 L. ed. 729, 739 (1900).

> form of statement the argument is this: There is property in the surface owners in the gas and oil held in the natural reservoir. Their right to take cannot be regulated without divesting them of their property without adequate compensation, in violation of the Fourteenth Amendment, and this although it be that if regulation cannot be exerted one property owner may deprive all the others of their rights, since his act in so doing will be *damnum absque injuria*. This is but to say that one common owner may divest all the others of their rights without wrongdoing, but the lawmaking power cannot protect all the owners in enjoyment without violating the Constitution of the United States."[47]

Since that time the doctrine has been followed by the Supreme Court of the United States in a number of instances.[48] The latest case is *Bandini Petroleum Co. v. Superior Court*,[49] wherein the Court said:

> "If the statute be viewed as one regulating the exercise of the correlative rights of surface owners with respect to a common source of supply of oil and gas, the conclusion that the statute is valid upon its face . . . is fully supported by the decisions of this court."[50]

In the *Ohio Oil* case[51] the Court, in saying that each landowner had an equal right to take whatever oil or gas he found under his land as long as waste was not committed, was applying the Rule of Capture. Indeed, it said:

> "It is also clear from the Indiana cases cited that, in the absence of regulations by law, every owner of the surface within a gas field may prosecute his efforts and may reduce to possession all or every part, if possible, of the deposits without violating the rights of the other surface owners."[52]

The *Bandini* case,[53] while not going as far as the *Ohio Oil* case, merely upheld a California statute prohibiting excess use and waste of the gas in a common reservoir. The owners of the surface had a correlative right to share in the reservoir energy, and waste thereof would cause loss to them of the amount of oil that could be recovered. Accord-

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[47] *Ibid.*

[48] Lindsley v. Natural Carbonic Gas Co. 220 U. S. 61, 31 Sup. Ct. 337, 55 L. ed. 369 (1911); Noble State Bank v. Haskell, 219 U. S. 104, 31 Sup. Ct. 186, 55 L. ed. 112 (1911); West v. Kansas Natural Gas Co., 221 U. S. 229, 31 Sup. Ct. 564, 55 L. ed. (1911); Bacon v. Walker, 204 U. S. 311, 27 Sup. Ct. 289, 51 L. ed. 499 (1907).

[49] 284 U. S. 8, 52 Sup. Ct. 103, 76 L. ed. 136 (1931).

[50] *Id.* at 22, 52 Sup. Ct. at 108, 76 L. ed. at 145.

[51] Ohio Oil Co. v. Indiana, 177 U. S. 190, 20 Sup. Ct. 576, 34 L. ed. 729 (1900).

[52] *Id.* at 208, 20 Sup. Ct. at 583, 34 L. ed. at 739.

[53] 284 U. S. 8, 52 Sup. Ct. 103, 76 L. ed. 136 (1931).

ingly, it is seen that while the correlative rights doctrine has been applied by the Supreme Court in upholding the statutes enacted to prevent waste, the doctrine has not been applied in an effort to determine the rights of the owners of the pool to its contents. For all intents and purposes, the Rule of Capture still governs with respect thereto.[54]

Forty years ago it was originally held that the state could legislate to prevent waste and secure an equitable distribution of the oil and gas in a common reservoir. States have legislated, and the state courts, too, have held such legislation constitutional; but still the same doctrine prevails with reference to the right to produce all the oil and gas possible.

In the "old days" "reservoir energy" was sometimes referred to as "rock pressure" and it was thought that the quicker the rock pressure was utilized, the greater the recovery of oil would be. This reasoning was based upon the fact that quite often when a gas well came in it was found that if the gas was blown off, the oil would follow. So it was reasoned that if they flowed the gas quickly, they would get an oil well.

Now, as a result of the research made by petroleum engineers and geologists, it is known that by reason of great pressure, considerable gas is held in solution with the oil, which decreases the viscosity of the oil and permits it to flow more readily, and through smaller pores of the formation in which it lies. Further, it is now known that when the gas is permitted to escape in great quantities, the other gas that has been in solution rises to fill the vacant pores, and leaves the oil more viscous. Such oil can then be recovered only by repressuring, a method exceedingly expensive and still not perfected. If, on the contrary, the well is so perforated that it will produce only from the portion of the sand containing oil, the escape of gas is slow, and it brings with it as much of the oil as it is mixed with. Further, the free gas, on the top of the structure, then mingles with the oil, downward, and assists in pushing it towards the perforated casing.

If forty years ago the Supreme Court could state that preservation of the reservoir energy was justified in order to protect the correlative rights of the owners of the pool, with the little knowledge of the correct facts about the production of oil then available; the scientific and practical knowledge obtaining today limits, in many instances, the need for the Rule of Capture.

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[54]Champlin Refining Co. v. Corp. Comm. of Okla., 286 U. S. 210, 52 Sup. Ct. 559, 76 L. ed. 1062 (1932); Sterling v. Constantin, 287 U. S. 378, 53 Sup. Ct. 190, 77 L. ed. 375 (1932).

The Change of Economic Conditions as a Basis of the Constitutionality of Conservation Statutes

Another rule of constitutional interpretation which has considerable weight in determining the legality of a police measure is the change in economic conditions. Such a change may lead to the upholding of a conservation statute today, where, under prior economic conditions, the measure would definitely have been considered an infringement of the due process clause of the Constitution; which is to say that, despite the considerable advancement in the science of the oil industry, understanding of the peculiarities or the behavior of oil and gas, underground, came slowly, and even now is not fully comprehended. Therefore, police measures regulating the manner and method of producing oil and gas which would have been unconstitutional several years ago might be held valid at the present time.

The petroleum industry had existed more than twenty years before the first regulatory statute was enacted in the United States. This statute was enacted in Pennsylvania,[55] and provided for the protection of oil and gas formations against water intrusion. About 1886 the State of Indiana developed one of the greatest gas fields ever discovered and used every means possible to insure the longevity of the supply for domestic and commercial use. The first real controversy between the policy of conservation and the policy of production arose out of the attempt of the State of Indiana to enforce this conservation statute. On one hand the proponents of conservation advanced the theory that the right to produce was subservient to the duty to the public not to waste natural resources. On the other hand the opponents of conservation insisted upon standing upon their legal rights to drill and produce oil and gas whensoever and howsoever they pleased. In *Townsend v. State*[56] a statute prohibiting the use of flambeau lights in the burning of gas was held constitutional as a legitimate exercise of the police power of the state. The landmark case was *Ohio Oil Co. v. Indiana,*[57] also involving the prevention of waste of gas. This case has been discussed elsewhere herein at length.[58]

In 1915 Oklahoma, having lost considerable oil through over-production, passed a far-reaching statute for the prevention of waste of oil.[59] In 1919 the Texas Legislature formulated and passed an act for the

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[55]Pa. Acts 1878, p. 190.
[56]147 Ind. 624, 47 N.E. 19 (1897).
[57]177 U. S. 190, 20 Sup. Ct. 576, 44 L. ed. 729 (1900).
[58]See *supra* page 369.
[59]Okla. State Laws 1915, c. 25.

prevention of waste of oil and gas and placed the enforcement of the act in the hands of the Railroad Commission.[60] The Federal Government, too, was looking into the question of undue waste and from 1917 on it published numerous tracts on the conservation of the reservoir energy of an oil pool in an effort to obtain the greatest possible recovery therefrom.[61] In December 1924 the Federal Oil Conservation Board was appointed by President Coolidge, with the following comments for the reason therefor:

> "It is evident that the present method of capturing oil deposits is wasteful to an alarming degree and it becomes impossible to conserve oil in the ground under present leading practices if a neighboring owner or lessee wishes to gain possession of the deposits."

This reference was to the evils brought about by the application of the Rule of Capture and the Offset Drilling Rule, and the economic evils resulting therefrom in the competitive drilling then going on of the type found in the Cushing, Seminole and Oklahoma City Fields in Oklahoma, the East Texas field, and the town lot area in the Los Angeles Basin, where each operator, regardless of the rights of his neighbors, sought to produce as much oil from his own property as he could.

Prior to the enactment of the NRA the four largest oil producing states had already put into force legislation for the conservation of the reservoir energy of its fields in order to obtain the largest possible ultimate recovery. Section 9 of the NRA indicated that the Federal Government would assist the states in their endeavor to conserve, and in the enforcement of their own statutes. That provision, however, was declared unconstitutional as an unlawful delegation of legislative power,[62] but a petroleum code had already been adopted by the Act, conferring the administration upon the Secretary of the Interior. A pertinent provision was "(a) That any and all wells hereafter drilled shall be located in accordance with a plan of well location approved by the Administrator. . . . (b) That for the purpose of more properly conserving the natural resources of the pool, the production of oil and gas therefrom (1) shall at all times be without waste, as defined by the law applicable; and (2)

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[60]Tex. Laws 1919, p. 285.

[61]Swigart and Bopp, *Experiments in the Use of Back Pressure on Oil Wells,* Department of the Interior Technical Paper 322 (1924); Swigart and Beecher, *Manual for Oil and Gas Operations,* Department of the Interior Bull. 232 (1923); Beal and Lewis, *Petroleum Technology,* Department of the Interior Bull. 194 (1921); *Method for Increasing Recovery from Oil Sands,* Bureau of Mines Bull. 148 (1917); Bull. 177 (1919).

[62]Panama Refining Co. v. Ryan, 293 U. S. 386, 55 Sup. Ct. 315, 79 L. ed. 444 (1935).

shall be limited so that gas will not be unduly wasted in or for the production of oil."

In 1929 a committee of nine of the American Bar Association was appointed to study the problems concerning the conservation of mineral resources. It recommended a compulsory state statute admirably suited to solve most of the problems incident to the conservation of reservoir energy for larger recovery.[63] The greatest difficulty encountered in enforcing the various state laws was the fact that most of the crude oil produced moved in interstate commerce. However, the Connally "Hot Oil Act" was enacted in February, 1935,[64] prohibiting the movement in interstate commerce of crude oil, or its products, where the same had been produced in violation of any state statute. Congress had also given its approval[65] and consent to an interstate oil compact, entered into by a number of the important oil producing states.[66]

Prior to 1924, when the Federal Oil Conservation Board was appointed, no serious effort had been made by the states to enact thorough and complete conservation statutes. The results of investigations made by the Bureau of Mines and the advancement of learning brought about by the establishment of schools of mines, geology and petroleum engineering in the various universities resulted in a system of public education that convinced even the most hard-headed oil operator that there were evils connected with the close spacing and competitive drilling methods that led to waste of reservoir energy and loss of recovery. The experience of operators in the Cushing, Seminole, Oklahoma City, East Texas and Los Angeles Basin fields was bearing fruit. Overproduction brought not only loss of reservoir energy and waste and smaller recovery, but also lower prices for crude. In 1931 the price of crude dropped to ten cents per barrel. Martial law was necessary to enforce the orders of the regulatory bodies of the states of Texas and Oklahoma. Out of these conditions, and others, came the modern era, characterized by the passage of well-considered, well-planned and comprehensive conservation laws.

It is with respect to this later era, the modern era, that circumstances show how much force must necessarily be given to the proposition that

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[63]See the REPORT OF THE COMMITTEE ON CONSERVATION OF MINERAL RESOURCES of the Section of Mineral Law of the American Bar Association, published by the Association January 14, 1929.

[64]49 STAT. 30 (1935), 15 U. S. C. A. § 715-715*l* (1934).

[65]Statutes at Large, 939, Joint Resolution No. 57, approved Aug. 10, 1937.

[66]Arkansas, Colorado, Illinois, Michigan, Kansas, Texas, Oklahoma, New Mexico. California signed the compact but never ratified such signing.

a change in economic conditions in the business of producing oil necessitates a change in the type of police measure put into force. This new type of police measure must be capable of withstanding any and all attacks upon its constitutionality on the grounds that it violates the due process clause. In Indiana the early conservation laws dealt with gas alone, and, in fact, most of the conservation statutes prior to 1927 referred to gas, and only gas, for two reasons. In the first place, gas was more volatile than oil; and, in the second place, the underground relationship between gas and oil was inadequately understood, if understood at all. In 1923 Arkansas applied the acreage factor to gas production. Under the terms of the act[67] not only was the gas production limited to prevent waste, but ratable taking was also provided for.[68] In 1924 the Legislature of Louisiana made a somewhat different approach to the spacing problem in connection with its oil wells. Wells drilled on small tracts were penalized as to allowable production as against wells drilled on larger tracts.[69] In 1929 Michigan enacted a gas well spacing act[70] somewhat similar to the Arkansas statute referred to. In 1932 Mississippi passed an act placing a specific penalty on gas wells drilled on small tracts.[71] These statutes were predecessors to the general statutes against waste of every kind, either of oil or of gas. In almost every one of the major oil producing states, there have come into being statutes protecting the reservoir energy against depletion, waste and excessive use.[72] In addition to such statutes almost every one of those

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[67]Ark. Laws 1923, p. 556.

[68]*Ibid.* In providing for ratable taking of gas this clause was added: ". . . having due regard to the acreage drained by each well in such a manner as to prevent any person, firm or corporation securing an unfair proportion of the gas in the pool."

[69]La. Acts 1924, No. 252, La. Gen. Stat. Ann. (Dart, 1932) §§ 4771-4783.

[70]Mich. Pub. Acts 1929, No. 9.

[71]Miss. Laws 1932, c. 117; Miss. Code Ann. (Supp. 1938)c. 166B.

[72]*Arkansas:* Ark. Dig. Stat. (Pope, 1937) § 10465-77, revised by Act 105, 1939. *California:* Cal. Stat. 1915, c. 718, amended by Cal. Stat. 1929, c. 535, p. 923 and Cal. Stat. 1931, c. 791, p. 1644. The constitutionality of the 1929 statute was upheld in Bandini Petroleum Co. v. Superior Court, 284 U. S. 8, 52 Sup. Ct. 103, 76 L. ed. 136 (1931), and People v. Associated Oil Co., 211 Cal. 93, 294 Pac. 717 (1930), *aff'd,* 212 Cal. 76, 297 Pac. 536 (1931). California's latest attempt at a general conservation law was defeated in 1931 when the 1931 Statute, c. 585, was voted down at a referendum May 3, 1931. *Colorado:* Colo. State Law 1933, c. 137. *Kansas:* Kan. Laws 1931, c. 226 (oil proration), amended by Kan. Laws 1933, c. 213 (oil proration), and Kan. Laws 1935, c. 213 (gas proration). Kansas has neither over-production nor waste, yet it reacted to the influences that were bringing about the enactment of comprehensive conservation statutes in other states and enacted its own. *Kentucky:* Ky. Codes Ann. (Carroll, 1932) Civ. Prac. § 3766-21, amended by Ky. Acts 1936, c. 35, p. 88. *Louisiana:* La. Gen. Stat. Ann. (Dart, 1932) § 4754; La. Gen. Stat. Ann. (Dart, 1932) § 4765.5; La. Gen. Stat. Ann. (Dart, 1932) §§ 9482.1, 9482.16. *Michigan:* Mich. Comp. Laws (1929), No. 15 (oil and gas); Mich. Comp. Laws (1937), No. 326 (gas). *Mississippi:* Miss. Laws 1932, c. 117, Miss. Laws 1934, c. 154, Miss. Laws 1936, c. 305, Miss. Code Ann. (Supp. 1938) c. 166B. *Montana:* Mont. Rev. Codes

states has attempted to control production, prevent waste, and restrain unnecessary drilling by the enactment and enforcement of well spacing legislation.[73]

Well spacing has now become of great importance in controlling the efficiency of operations in a common pool or reservoir. It has been proven beyond doubt that close spacing is not necessary for the proper drainage of the reservoir. In fact, close spacing reduces the ultimate recovery from the reservoir, as it brings on a reduction in reservoir pressure due to the inefficient utilization of the reservoir energy.

All in all, these statutes have shown the concerted and unqualified effort on the part of the states to prevent waste, increase the life of the fields within their confines, and obtain the greatest possible ultimate recovery therefrom. In some states the desired results have been obtained with little or no litigation involving the enforcement of the statute, or questioning its constitutionality. In other states the fight has been bitter. The doctrine of correlative rights was recognized early in the struggle even in instances where there was no statutory provision for their enforcement.[74] In more recent years any number of cases have upheld the doctrine in supporting the constitutionality of conservation

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ANN. (Anderson & McFarland, 1935) § 3554; Mont. Laws Ex. Sess. 1933, c. 18. *New Mexico:* N. M. Laws 1935, c. 72. *Oklahoma:* Okla. State Laws 1933, c. 131; Okla. State Laws 1935, c. 59. The constitutionality of this statute was upheld in the now famous case of Patterson v. Stanolind Oil & Gas Co., 305 U. S. 376, 59 Sup. Ct. 259, 83 L. ed. 231 (1938). *Texas:* TEX. STAT. (Vernon, 1936) Art. 6004-66. *West Virginia:* W. VA. CODE ANN. (Michie & Sublett, 1937) § 2477 *et seq.* *Wyoming:* WYO. REV. STAT. ANN. (Courtright, 1931) § 78-301, amended by Wyo. Laws 1933, c. 81.

[73] *Arkansas:* Ark. Laws 1939, Act 105. *California:* Cal. Laws 1931, c. 568. *Kansas:* Kan. Laws 1935, c. 213: *Louisiana:* LA. GEN. STAT. ANN. (Dart, 1932) §§ 9482.1-9482.16. The constitutionality of this act was upheld in Lilly v. Commissioner of Conservation, 29 F. Supp. 892 (1939). *Michigan:* MICH. COMP. LAWS (1929) § 5704. *Montana:* MONT. REV. CODES ANN. (Anderson & McFarland, 1935) § 1882.11. *New Mexico:* N. M. STAT. ANN. (Courtright, Supp. 1938) § 97-810. *Oklahoma:* Okla. Laws 1933, c. 131, amended by Okla. Laws 1935, c. 59. *Texas:* TEX. STAT. (Vernon, 1936) Art. 6014, and the well spacing rules of the Railroad Commission, No. 9 and No. 37. *Wyoming:* Regulations 2 c. Attention must be called to several city ordinances enacted for the purpose of regulating well-spacing. The City of Oxford, Kansas, enacted an ordinance which was upheld in Marrs v. City of Oxford, 24 F.(2d) 541 (D. Kan. 1928), *aff'd,* 32 F.(2d) 134 (C.C.A. 8th, 1929). Chase, Kansas, had a similar ordinance which was upheld in Helmerick & Payne v. Roxana Petroleum Corp., 136 Kan. 254, 14 P.(2d) 663 (1934). An Oklahoma City ordinance of like effect was upheld in Anderson-Kerr v. Van Meter, 162 Okla. 176, 19 P.(2d) 1068 (1933).

[74] Manufacturers Gas & Oil Co. v. Indiana Natural Gas & Oil Co., 155 Ind. 461, 57 N.E. 912 (1900); Louisville Gas Co. v. Kentucky Heating Co., 117 Ky. 71, 77 S.W. 368 (1903); Higgins Oil and Fuel Co. v. Guaranty Oil Co., 145 La. 233, 82 So. 206 (1919); Ross v. Damm, 278 Mich. 388, 270 N.W. 722 (1936).

statutes,[75] while the most recent trend seems to rely more and more upon the police power of the state, acting for the protection of the public interest and welfare, as the most sound and logical basis for upholding such statutes.[76] The Federal Courts have advanced a theory that the states do not have the right to legislate for the protection of the correlative rights, apart from injury to public interest and welfare caused by waste.[77] Their reasoning is that the doctrine as set forth in the *Ohio Oil* case has been used only as a part of the theory of the police power of a state acting in the public interest. In view of the more recent decision of *Erie Railroad Co. v. Tompkins*[78] it is not known what the Federal Courts would now hold.

The evils of over-production and waste prior to the enactment of comprehensive and modern conservation statutes are so self-evident and so well known that it is of little need to mention them at length herein. Experience in Arkansas offers the best example of what can happen when proper conservation statutes are not enacted. As early as 1888 there was gas discovered in Arkansas. After the turn of the twentieth century there were a number of gas fields in the western portion of the state. The operation of these fields was orderly, and what is astounding is the fact that there was no litigation relative to the waste of the gas. The fields were developed conservatively. In 1917 the first Gas Conservation Act was passed,[79] due, not to the over-production and

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[75]Patterson v. Stanolind Oil & Gas Co., 305 U. S. 376, 59 Sup. Ct. 259, 83 L. ed. 231 (1938); Thompson v. Consolidated Gas Utilities Corp., 300 U. S. 55, 57 Sup. Ct. 364, 81 L. ed. 510 (1937); Champlin Refining Co. v. Corp. Comm. of Okla., 286 U. S. 210, 52 Sup. Ct. 559, 76 L. ed. 1062 (1932); Bandini Petroleum Co. v. Superior Court, 284 U. S. 8, 52 Sup. Ct. 103, 76 L. ed. 136 (1931); Henderson v. R. R. Comm. of Tex., 56 F.(2d) 218 (W. D. Tex. 1932); Marrs v. City of Oxford, 24 F.(2d) 541 (D. Kan. 1928), *aff'd*, 32 F.(2d) 134 (C.C.A. 8th, 1929); Oxford Oil Co. v. Atlantic Producing Co., 22 F.(2d) 597 (C.C.A. 5th, 1928); People v. Associated Oil Co., 211 Cal. 93, 294 Pac. 717 (1930), *aff'd*, 212 Cal. 76, 297 Pac. 536 (1931); Wilcox Oil & Gas Co. v. Walker, 168 Okla. 355, 32 P.(2d) 1044 (1934); Russell v. Walker, 160 Okla. 145, 15 P.(2d) 114 (1932); Julian Oil & Royalties Co. v. Capshaw, 147 Okla. 237, 292 Pac. 841 (1930); Peterson v. Grayce Oil Co., 37 S.W. (2d) 367 (Tex. 1931.)

[76]Amazon Petroleum Corp. v. R. R. Comm. of Tex., 5 F. Supp. 633 (E. D. Tex. 1933); Danciger Oil & Refining Co. v. Smith, 4 F. Supp. 236 (E. D. Tex. 1933); Constantin v. Smith, 57 F.(2d) 227 (E. D. Tex. 1932); People's Petroleum v. Sterling, 60 F.(2d) 1041 (E. D. Tex. 1932); People's Petroleum Producers v. Smith, 1 F. Supp. 361 (E. D. Tex. 1932); Brown v. Humble Oil & Refining Co., 126 Tex. 296, 83 S.W.(2d) 935 (1935); Danciger Oil & Refining Co. v. Railroad Commission, 49 S.W.(2d) 837 (Tex. 1932).

[77]Consolidated Gas Utilities Co. v. Thompson, 14 F. Supp. 318 (W. D. Tex. 1936); Texas Panhandle Gas Co. v. Thompson, 12 F. Supp. 462 (W. D. Tex. 1935); Canadian River Gas Co. v. Terrell, 4 F. Supp. 222 (W. D. Tex. 1933); Texoma Natural Gas Co. v. Terrell, 2 F. Supp. 168 (W. D. Tex. 1932).

[78]304 U. S. 64, 58 Sup. Ct. 817, 82 L. ed. 787, 114 A. L. R. 1487 (1938).

[79]Ark. Laws 1911, Act 166.

wanton waste, but primarily to inexperience on the part of the developers of the fields. After the passage of the act the inexperienced operator profited by the rules and regulations established. The right of the state to regulate the production of gas was never questioned. Oil was discovered in the state thereafter. The conservation statutes enacted prior to the finding of oil dealt with the production of gas only. There was no attempt to regulate the production of oil, as it was not contemplated at that time. Accordingly, the manner in which the fields were run, the method of production and operation, was a disgrace to the industry. El Dorado and Smachover ran wild. Oil flowed everywhere, polluting the streams, going to waste. The supply was tremendous, and method of disposal poor. Prices went down, the field reservoirs were dissipated. There was waste, above and below the ground. A conservation statute to protect the state and its resources was necessary and was enacted in 1923.[80]

Compare, then, the evils attendant to the production of oil where there was no regulatory statute, and the reasonable, safe and sound practice *in the same state* growing out of the production of gas under a fair conservation statute. What better incentive to the enactment of such statutes is needed?

Conclusion

It is quite obvious that concerted drilling of a common source of supply at any one point operates to release the reservoir pressure more rapidly at that point, thereby creating and resulting in an uneven and non-uniform use of the reservoir energy; with the result that other parts of the oil producing structure or formation do not receive the same benefit from the common reservoir as would be accomplished by the regular and uniform spacing of wells. Waste, therefore, results, since oil is permanently left in the oil bearing sand which cannot be produced by mechanical means because of the loss of the permeability in the structure, and the increase of fluid viscosity.

The theory and principle upon which the modern conservation legislation is enacted is to require a uniform use of the natural gas which constitutes the reservoir pressure by which the oil is lifted from the subterranean formations of the earth to the earth's surface. Such legislation must be predicated upon the engineering principle, well demonstrated and well recognized by the courts as well as by the various state departments charged with the duty of enforcing the conservation stat-

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[80]Ark. Laws 1923, Act 664.

utes, rules and regulations of such state, that the most efficient use of the reservoir energy would result in the largest ultimate recovery of oil from the oil-bearing sands. Such legislation must further be predicated upon the fact that there is now available testimony to find and determine the space or area that will be most efficiently drained of oil by one well. It is a well established petroleum engineering principle that the regular and uniform spacing of wells will result in the even and uniform utilization of the reservoir pressure, and, therefore, will result in an orderly and uniform use of such reservoir energy, whether the same be due to the presence of gas or water; so that when the available reservoir energy has been exhausted, the maximum quantity of oil will have been lifted from the subterranean formations to the resultant benefit alike or all minerals owners, lessees, the state and the general public.

The modern theory of oil conservation, then, is a theory based upon the right of sharers of a common reservoir to take equitably therefrom in a way so as to prevent waste of reservoir energy, and to obtain the greatest ultimate recovery therefrom. This theory is based upon sound geological data, clear legal principles, wise economic policies and thorough business methods. If the courts should sanction what the legislatures have done towards carrying into execution this theory, the petroleum industry would enjoy a fair and reasonable degree of prosperity. Producers of crude oil are willing and, indeed, anxious to supply the market with its reasonable demand for petroleum. However, they clearly recognize the fact that the best storage space for excess crude is in the ground, where it is stored by nature. They do not want to engage in another struggle as a result of over-production. In the oil industry alone, where natural conditions are such as they are, one man, or a limited few, by excessive production under the Rule of Capture can force the entire industry into a similar state of over-production. The salvation of the industry lies in the willingness of each and every operator to permit each to enjoy that which belongs to him. This has not been accomplished without laws, and so the petroleum industry must submit to regulations. However, it is to the interest of the industry, the state, and the landowners to secure such regulations as are fair and reasonable.

OIL CONSERVATION: STATUTES, ADMINISTRATION, AND COURT REVIEW

*Robert E. Hardwicke**

In February, 1940, a subcommittee, usually known as the Cole Committee, of the Committee on Interstate and Foreign Commerce, House of Representatives, held hearings in Washington in connection with proposed legislation providing for extensive regulation by the Federal Government of the oil industry. At these hearings, many witnesses appeared in behalf of the industry. Apart from the introductory and concluding portion hereof, and from a few additional footnotes, this article is composed of Sections IV and V of the paper by the author hereof presented at the hearings in February, 1940, under the title *Phases of Legal History and Practical Operation of Conservation of Oil by the States in Relation to Ascertainment of Limits of Desirable Program of Assistance by the Federal Government.* The complete paper appears in the published record of the hearings.[1] Much of the material was taken from *Legal History of Conservation of Oil and Gas, A Symposium,* published in 1939 by the Section of Mineral Law, American Bar Association.

In the paper prepared for the hearings before the Cole Committee, Section II dealt with the early conservation laws and methods, and Section III with modern statutory law and its growth. Such material constituted the background for Sections IV and V which have been used as the body of this article.

For convenience, the section numbers and the footnote numbers as they appear in the Cole Committee paper have been changed. No changes have been made in the text or in the footnotes; however, a few additional footnotes have been added in order to give reference to important events occurring since February, 1940. Where new footnotes are added, the footnote reference number is enclosed in brackets; where new material is inserted in the original footnotes, only the new material is enclosed in brackets.

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[1]Part 4 (Petroleum Investigation), *Hearings before Subcommittee of the Committee on Interstate and Foreign Commerce, House of Representatives, on H. R. 290 and H. R. 7372,* 76th Cong., 3rd sess. (1940). Copies of this volume may be had from the Superintendent of Documents, Washington, D. C., at a cost of 75¢ per volume.

I. Similarity of Existing State Statutes

A. *Compilations and Digests*

The conservation statutes in the various states are found in Volume 5 of Summers, *The Law of Oil and Gas* (Perm. ed. 1939), including pocket parts, and in Volumes 4 and 5 of Thornton, *The Law of Oil and Gas* (1933) including pocket parts or supplements. A rather comprehensive digest of the existing statutes, compiled by Earl Foster and James C. Hamill, of Oklahoma, begins on page 283 of *Finding and Producing Oil,* a volume published by the American Petroleum Institute in 1939. Comparison of the conservation statutes and regulations of seven states appears in tabular form, page 206 *et seq.* of *Energy Resources and National Policy,* a report of the Energy Resources Committee to the National Resources Committee, published in 1939 by the National Resources Committee, of Washington, D. C.

Reference is again made to *Legal History of Conservation of Oil and Gas, A Symposium,* which gives the status of legislation in the nine states covered as of January 1, 1939.

B. *Fundamentals of State Statutes*

1. Waste Defined and Prohibited

The statutes prohibit waste which is by them usually defined in both general and specific terms, frequently including, as a specific definition, production in excess of reasonable market demand.

2. Administrative Agency Created

The typical act creates an administrative agency which is authorized to promulgate rules, regulations and orders reasonably necessary to make the law effective. There are various types of administrative agencies; for instance, in Texas the members of the agency are elected by vote of the people; in Arkansas the members are appointed by the Governor; while in New Mexico the agency is composed of the Governor, the Commissioner of Public Lands and the State Geologist.

In most of the early cases in which the validity of the conservation statutes or the regulation was under attack, the point was usually raised that legislative authority had been delegated to the administrative agency; however, the courts consistently held that the statutes were constitutional in as much as sufficient standards had been established by the legislature, leaving to the administrative agency nothing but administrative functions.[2]

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[2] 1 Summers, Oil and Gas (Perm. ed. 1938) 290, § 106, n. 35 lists many cases.

3. Hearing and Notice as Basis for Regulations

On the whole, the statutes contain provisions which provide for notice and a hearing before the administrative agency issues its regulations. Most of these statutes provide that any interested party has the right to appear and be heard, to introduce evidence and otherwise to participate in the proceeding so that his viewpoint may be fully developed. Whether due process of law requires notice and a hearing as pre-requisites to a valid regulation, apart from a statutory provision to that effect, need not be discussed here.[3] Regardless of statutory mandate for notice and hearing, such would surely be given in order to cut off any question of invalidity for failure so to do, as well as to escape the criticism of conducting star-chamber proceedings.

4. Distribution of Allowable

The statutes, on the whole, provide in general language for distribution of the allowable for a field among the operators. Experience has shown that, because of great differences in physical conditions in fields, the legislature cannot write a proration formula which will fit each field. Whatever the legislature may set forth as a general standard, such as that the distribution must be "on a reasonable basis" (Texas act), or whether *any* general standard be given, it seems to be clear that the due process and equal protection clauses of the 14th Amendment to the Constitution of the United States stand in the way of the enforcement of any distribution, though it be required by statute, which takes the property of one operator for the benefit of another. This general subject will be discussed in some detail under Subsection 5 of Section C which follows.

5. Court Review

Elaborate provision is usually made for court review. The method followed in Oklahoma, which authorizes the Supreme Court to act administratively, is, at least in theory, quite different from the practice followed in the other states. The usual method is to provide for a test of the validity of the law or any regulation thereunder by an injunction suit, with the trial being *de novo*. Most of the statutes provide that the statutes, and the rules, regulations and orders are *prima facie* valid.

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[3]Morgan v. United States, 298 U. S. 468, 56 Sup. Ct. 906, 80 L. ed. 1288 (1936), *on second appeal,* 304 U. S. 1, 58 Sup. Ct. 773, 82 L. ed. 1129 (1938), *on reh.,* 304 U. S. 1, 58 Sup. Ct. 999, 82 L. ed. 1135 (1938), contains language which apparently supports either argument. See comment in Hardwicke, *Legal History of Conservation of Oil in Texas,* in LEGAL HISTORY OF CONSERVATION OF OIL AND GAS, A SYMPOSIUM (1938) 260, n. 55.

It appears that no statute specifically undertakes to declare what is the proper function of a court in testing the validity of a statute or an order thereunder. Lawyers are now debating the interesting question whether, *in a case involving a claim of confiscation as being contrary to the due process clause of the 14th Amendment to the Federal Constitution,* the court should make an independent determination of the facts as well as pass upon legal points or whether the court, with respect to fact issues, must, sustain the action of the administrative agency if there be substantial evidence in support.

A very strong argument can be made in favor of the contention that the court is under the duty to make independent findings in a case involving the constitutional question of confiscation, whether or not the statute specifically requires such action of the court. A brief discussion of that subject will be found under Subsection D of Section II hereof.[4]

C. *Subjects of Special Interest*

Most of the discussion of regulation centers around at least one of the following subjects: (a) Rule of capture; (b) Market-demand limitation; (c) Economic waste; (d) Optimum rate of flow; (e) Distribution of allowable production among field and among operators in the field; (f) Proration; (g) Pooling of tracts; and (h) Unit Operations. Each of these subjects will be briefly discussed, for the points to be made are applicable to either state or federal statutes.

1. Rule of Capture

No discussion of regulation of production can continue long without bringing in the "rule of capture." The "rule of capture" or "law of capture" is probably the most mis-used and mis-understood term in the entire phraseology of oil conservation. Nearly all evils are attributed to the rule of capture, and it is the standard alibi which is relied upon to prove innocence of voluntary wrong-doing. Different persons not only have different concepts, but the same person in a short space of time will use the term with different meanings. Three conflicting concepts are stated:

> a. The "rule of capture" or the "law of capture" is a rule of law arising from ownership of property, or the right to produce oil and gas, by virtue of which an operator may

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[4]As will appear from the discussion in note [15] *infra* and in the concluding remarks to this discussion, page 414 *infra,* the Supreme Court seems to have held recently that the federal courts should not interfere with state administrative agencies except in extreme cases.

drill and produce as he pleases, regardless of the effect on his neighbors, and with no liability whatever should he produce oil which was drained from under his neighbors' lands. In a broad sense, the rule of capture is used to mean a condition where there is no control by a regulatory agency, and particularly no proration or restriction on production.

Obviously, if the rule of capture means what has been stated in the preceding sub-paragraph, then conservation laws, particularly if proration takes place, materially modify or annul the rule.

b. The "rule of capture", under a strict, legal interpretation, is a rule of law (sometimes called rule of convenience) arising from ownership of property, or the right to produce oil and gas, by virtue of which an operator who drills on his own land, or land held under an oil and gas lease or other instrument, acquires title to the oil which he legally produces from the well, whether or not drainage takes place from surrounding properties.

Under this second concept, the rule of capture is really nothing more than a rule of convenience, largely for quieting title to oil because of the difficulty of deciding definitely the original source of that oil, or the difficulty of conducting operations so that no oil will be produced except that originally under the tract. The rule of capture, under the second concept, is not abrogated by conservation statutes and proration orders, no matter how rigid the restriction may be; because, whatever amount of oil *is authorized* to be produced under the order distributing the allowable for the field belongs to the operator who produces it, at least as far as his neighbors are concerned, and whether or not it be reasonably certain that some of the oil was drained from neighboring lands. Pooling orders do, in a sense, modify the concept just stated. The rule of capture, as defined in sub-paragraph *b, supra,* does not, however, stand in the way of reasonable conservation measures.

c. The "rule of capture" is sometimes used as the antithesis of "ownership-in-place."

Frequently it is said that the field allowable should be distributed by taking into account the relative amounts of oil in place under each tract, this being the ownership-in-place method,

> as distinguished from "rule of capture," which, in the sense used, really means on the per-well method, or per-well-potential method, by virtue of which one tract gets a higher relative allowable than another, through the reserves or oil-in-place be the same.

The origin and true meaning of the rule of capture, its bearing on conservation statutes and distribution of allowable, and the effect, if any, of the holding in any particular jurisdiction as to ownership of oil in place, are all discussed at some length in an article by the writer, prepared in 1935, for the meeting that year of the Section of Mineral Law of the American Bar Association. The article was subsequently published in 13 *Texas Law Review* 391 (1935). There appears to be no need to digest the contents of the article, except to say that the second concept, stated above in paragraph *b,* was said to be the true one. The same general conclusions are stated in 1 Summers, *The Law of Oil and Gas* (Perm. ed. 1938), Sections 62 and 63.

Perhaps it would be well to add that the rule of capture is the same in all states, whatever the holding may be as to the ownership of oil in place, that it does not prevent the limitation of production; and, finally, that it does not justify regulations which, under similarity of conditions, gives one operator more than his fair share by causing reasonably avoidable drainage to his property.

2. Reasonable Market Demand

These words are frequently misunderstood. They were not defined in the Oklahoma statute of 1915, wherein they first appeared. In due course, however, the words came to have a very definite meaning, which may shortly be stated as being equivalent to "current consumption demand."

In the early days of production control, 1930 and 1931, the regulatory agencies in Oklahoma, Texas, Kansas and other states took the position that enormous amounts of oil were in storage, being far beyond any reasonable needs, and that this amount was increasing. It was argued that, even with the most modern methods of storage, there was considerable loss from fires, evaporation, leakage, and the like. All these conditions, it was said, brought about physical waste in material quantities.

Moreover, without production limitation, it was pointed out that many operators could not produce to capacity as some of their neighbors were doing, because the former had no market for all the oil, and could not store it unless pit or open earthen storage was used. The result

was that those operators who had markets or storage produced to capacity, while their neighbors' wells were entirely shut in, or were producing much less than capacity, with drainage taking place. Obviously all manner of complications arose, including what is generally termed "lack of ratable production."

The engineers testified that ratable production or withdrawals was to be distinguished from spotted or concentrated withdrawal; that, when ratable production existed, each operator or property produced relatively with others in the field; though not equally per well, and that there was a reasonably uniform use of reservoir energy, and a relatively uniform rise of any water table, with no abnormal differences in pressure and no heavy withdrawals in localized areas which tended to cause dissipation of energy and improper water encroachment. The lack of ratable production was clearly demonstrated as being one of the causes of underground waste.[5] It appeared to be clear that, if it were possible to determine within reasonable limits the current consumptive demand for oil, then a restriction of production to that figure, followed by a proper distribution of the allowable, would tend to give each operator a market for his production, and would prevent further unreasonable additions to storage—all to the end of preventing physical waste above ground, and of bringing about more ratable production, thereby decreasing the amount of underground waste.

Of course, in the early days of control there was considerable difficulty in finding with accuracy the consumptive demand, not only for the nation, but for the individual states and areas. For a time, some of the regulatory agencies, in fixing allowables, gave too much reliance to so-called "nominations" of purchasing companies. These nominations were merely estimates or statements of the amounts of oil which the companies thought they wanted to purchase for the ensuing period of 30 to 90 days. Obviously, if nominations alone were considered and followed, the purchasing companies could, in a sense, fix the allowables, making oil scarce or plentiful, and discriminating against fields or areas, by nominating much or little, as they pleased, to be purchased where they pleased. Before very long, it became apparent that factors other than mere nominations should be considered, such as (a) past experience, (b)

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[5]See cases cited in notes 7 and 8 *infra,* particularly Danciger Oil & Refining Co. v. Railroad Comm. of Tex., 49 S.W.(2d) 837, 842 (Tex. 1932), and also Peoples Petroleum Producers v. Smith, 1 F. Supp. 361, 363 (E.D. Tex. 1932). Legal and engineering concepts of "ratable production" are given in *Legal Phases of Well Spacing* in Proceedings of Eighth Mid-year Meeting of the American Petroleum Institute (1938) Section I-General, ¶ 7.

whether storage of oil in certain areas was decreasing or increasing, (c) whether there was any difficulty in keeping wells connected to pipe lines or in getting connections for new wells, and (d) whether there was any reasonable need for all the oil nominated.

Beginning in 1933, the United States Bureau of Mines began to make estimates of current consumptive demand. These estimates were used as a basis for regulations under the Petroleum Code formulated under the National Industrial Recovery Act, and were also transmitted to the various state agencies to be considered by them with other evidence in determining the consumptive demand in each state. It was found that the United States Bureau of Mines could forecast with extraordinary accuracy the amount of gasoline and other petroleum products which would be consumed in the United States, and which would be needed to meet export demands. These data made it possible to calculate the crude oil needed to supply this demand. The process used by the Bureau of Mines, already described in these headings,[6] is fairly complicated; but in substance it is based upon the estimate of the number of motor vehicles which will be in use and the amount of gasoline they will consume, together with estimates of imports and exports.

Regulatory agencies have in general consistently undertaken to keep production from exceeding the current consumptive demand or reasonable market demand, declaring that this is a reasonable and proper method of preventing physical waste, both above ground and underground. The Supreme Court of Oklahoma, the Supreme Court of the United States, and the Court of Civil Appeals, Third District of Texas, have so held.[7] A three-judge federal court in Texas, in the *Macmillan* case, held, in 1931, that limitation of production to reasonable market demand, at least in the East Texas Field in view of the facts proved, had no reasonable relation to the prevention of physical waste. However, a similar three-judge court, in the second *Danciger* case, sustained in June, 1933, an order of the Railroad Commission of Texas covering the Panhandle Field, on the ground that the order prevented physical waste, and that it appeared that the production of the field had been limited to a figure found by the Railroad Commission of Texas to constitute the reasonable market remand for oil in the Panhandle Field.[8]

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[6]Testimony by H. A. Breakey, Nov. 7, 1939, especially that beginning at page 180 of the record of the hearing as printed for the use of the Committee on Interstate and Foreign Commerce.

[7]Champlin Refining Co. v. Corporation Comm. of Okla., 286 U. S. 210, 52 Sup. Ct. 559, 76 L. ed. 1062 (1932); Julian Oil and Royalty Co. v. Capshaw, 145 Okla. 237, 292 Pac. 841 (1930); Danciger Oil & Refining Co. v. Railroad Comm. of Tex., 49 S.W.(2d) 837 (Tex. 1932).

[8]Danciger Oil & Refining Co. v. Smith, 4 F. Supp. 236 (N.D. Tex. 1933); MacMillan v. Railroad Comm. of Tex., 51 F.(2d) 400 (W.D. Tex. 1931).

It may be said, therefore, that the actual interpretation of "reasonable market demand" by the various state agencies, plus the decisions in the cases mentioned, plus long continued usage in the industry, have brought about a meaning which is equivalent to "current consumptive demand."

The New Mexico statute passed in 1935 defines the words "reasonable market demand"

> "to mean the demand for such crude oil for reasonable current requirements for current consumption and use within or outside the state, together with the demand for such amounts as are reasonably necessary for building up or maintaining reasonable storage reserves of crude petroleum oil or the products thereof, or both such crude petroleum oil and products." [N. M. Laws 1935, c. 72, § 2 (c).]

This statutory definition conforms to the meaning which was well established at the time the statute was passed. The Legislature of New Mexico thought it advisable, however, to define the term so that there could be no question as to the sense in which it was used.

It is frequently argued that limitation to reasonable market demand, even if that be taken to mean current consumptive demand, is, after all, nothing but a price fixing or stabilization measure. A short answer to that contention is that the courts have held to the contrary, or at least have said that limitation to reasonable market demand is a proper and effective way to prevent physical waste above ground and underground; consequently, in the absence of a statutory prohibition, such as once existed in Texas, a regulatory agency is fully justified, as a waste-prevention measure, in keeping production from exceeding the reasonable market demand. The courts say that the effect, if any, upon price by such a restriction is a mere incident to the legal exercise of police power to prevent physical waste, and the regulation is not void as a price fixing scheme simply because there may be an incidental effect upon the price.[9]

For that matter, even if the right to limit production to reasonable market demand should be exercised by any state agency to fix an allowable *below the true demand in an effort to raise prices,* it is not at all certain that any such result would follow. Too many things could happen which would offset the effect of a temporary scarcity in that state. It may here be observed that, as a rule, the state commissions have been inclined to place the allowables too high, rather than too low.

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[9]Cases are cited in note 7 *supra.* See also State v. Associated Oil Co., 211 Cal. 93, 294 P.(2d) 717 (1930).

Another point may be made. Experience has shown that whenever production materially exceeds the reasonable market demand, prices are likely to drop so low that wholesale abandonment of small wells takes place, and they must be plugged. The great reserve which would normally be produced by these wells is wasted, for the cost of redrilling the wells would not be justified. No one contends that national or state allowables should be unduly restricted with the hope that prices will go so high that no small wells will be abandoned. It is argued, however, that unrestricted or excessive production will cause premature abandonment of small wells, with consequent physical waste. It seems advisable to keep production within consumptive limits, giving the small wells a chance to produce their reserves.

There appears to be nothing unusual in authorizing limitation to reasonable market demand. There is nothing in 10 years' experience which shows that the regulatory agencies have consistently or even frequently abused the power to prevent production from exceeding reasonable market demand. It may be admitted, however, that, by concerted action of all the regulatory agencies, a temporary scarcity could be brought about by the fixing of inordinately low allowables, resulting in a species of price fixing; but it is reasonably clear that the danger of such action is not great enough to cause alarm or to justify federal regulation. Such manipulation, if attempted for longer than a short period, or if attempted more than once or twice, would be met by political, legal and economic forces sufficient to prevent a similar occurrence or any success for the unwarranted program.

3. Optimum Rate of Flow

Within the last few years the suggestion has been frequently repeated that limitation of production to reasonable market demand should be discarded for a more scientific method which is termed "optimum-rate-of-flow method." In support of the recommendation, it is sometimes argued that fixing allowables for fields at the market demand more frequently than not causes, rather than prevents, physical waste, inasmuch as the efficient point of production is frequently below the figure representing the market demand. It is argued that engineers ought to make extensive tests in each field determining the most efficient rate of flow by taking reservoir pressure tests, water encroachment tests, gas-oil ratio tests, and the like, and then fix the allowable accordingly, irrespective of the market demand factor. It has been assumed by some of those who favor the optimum-rate-of-flow method that the total of the allowables fixed for the fields as a result of the suggested method will be substan-

tially the same figure which represents the reasonable market demand for the nation as now estimated by the United States Bureau of Mines. Apparently it has been assumed that the allowable production in some fields will be cut, being offset by increases in others, but that the total for the nation will be about the same as under the present system. The scientific character of, and the benefits to be derived from, the new program have been repeated so many times that they are frequently accepted as having been fully established by the facts.

It appears that those proposing the optimum-rate-of-flow method make collectively several erroneous assumptions. In the first place, not one of the statutes *requires* that the allowable for any field be fixed at a figure which would represent the field's share of the state market demand, regardless of any other factors. The statutes simply say that production in *excess* of the reasonable market demand is wasteful, which, as we have seen, is unquestionably a fact. In practice, regulatory agencies very frequently fix allowables for fields below what would be the figure if market demands only had been considered, taking the position that, if production should be permitted at the market demand figure, then underground waste would take place. Probably the most outstanding example of such a course is the East Texas Field. For years, the allowables for the field have been fixed by consideration of reservoir pressure declines, with little or no attention being paid to the market demand factor. On the other hand, there are fields in Texas, which, considering underground conditions alone, could produce much more oil than they are permitted to produce. Conroe and Yates are outstanding examples. If the optimum-rate-of-flow method should be used, the allowables from Conroe and Yates would be materially increased. The Railroad Commission of Texas has, however, determined for Conroe and Yates the share of each in the state's market demand; and, as a consequence of applying the market demand factor, the fields have been cut below the figure representing the maximum which they could produce without underground waste, provided, of course, ratable production would continue in the face of inability of the market to absorb the additional oil produced at the optimum rate. It should here be observed that little or no waste takes place in Conroe and Yates, though reduced *below* the maximum point which could be produced without causing underground waste. If any waste occurs, it has been considered to be less than that which would be caused if these two fields, as well as all other fields in the state, should produce in excess of the reasonable market demand.

Theoretically, in each field, the optimum-rate-of-flow figure or the market demand figure is selected, whichever may be the lower. Within reasonable limits, such has been the practice in most instances.

The proponents of the optimum-rate-of-flow method apparently assume that all would be well if each field throughout the nation should be fixed at the maximum which it could produce without causing physical waste underground. No one has published any figures which tend to prove such a statement. It may be that the assumptions are justified, and that the use of the optimum-rate-of-flow method would be as satisfactory or even better than the present method. On the other hand, it may be that, under application of the optimum-rate-of-flow method, the total production would be far in excess of the reasonable market demand. If so, physical waste above ground and underground would take place for the reason that there would be excessive and wasteful storage or else the operators in each field could not continue to produce at the ideal rate of flow, having insufficient storage, insufficient markets, and insufficient pipe line connections. Ratable production, which is a prime factor in preventing waste, would shortly be upset; and, though there might be allowables and proration schedules which would permit ratable production at an amount not to exceed the optimum figure, the facts would be that the producers could not follow the schedules.

Moreover, the proponents of the optimum-rate-of-flow method must necessarily assume that, after the scientific maximum for each field had been determined, the oil available for the markets would be of the right grade and character, and would be located at the proper places. It is not clear that such assumptions are justified. For instance, as an assumption only, the allowables for some fields in New Mexico, the Panhandle and West Texas might be increased enormously, thus producing for the market a large amount of sour oils or oils with a sulphur content. On the other hand, allowables for fields in the Gulf Coast of Louisiana and Texas, which are close to tidewater and which have different types of desirable oils, might be greatly decreased. If such should be the facts, then the whole transportation and marketing setup would likely be seriously disturbed, having little or no relation to normal markets, refinery centers, adequate transportation facilities, or the like.

Beyond doubt, the regulatory agencies and operators should with some precision determine the maximum rate at which a field could produce without causing physical waste, and should take great care to see that the field should not be permitted to produce in excess of that figure, unless unusual circumstances existed. It has not been established that

such procedure has not been followed as a general rule. Regulatory agencies should, and frequently do, place the allowable for a field below the optimum-rate-of-flow figure whenever it is necessary so to do in order to prevent production in excess of the reasonable market demand.

It would be interesting to know what some of the proponents of the optimum-rate-of-flow method would recommend if, following the program, the production for the nation should be 25 per cent above the present level, or, conversely, if the production should be 25 per cent *below* the present level. Serious economic disorders, including changes in prices, might occur in either instance, and surely physical waste would take place if production should exceed by 25 per cent the present figure which represents consumptive demand.

In the light of known facts, there appears to be no need to discard consideration of reasonable market demand, adopting in lieu thereof optimum-rate-of-flow; and clearly the failure of state regulatory agencies to make such a change at this time does not warrant extensive regulation by the federal government.

4. Economic Waste

Economic waste, as that term is used in conservation statutes, or in connection therewith, has not been defined in any conservation statute. In a broad sense, economic waste means failure to obtain the maximum benefit from a commodity, or the employment of a commodity to an inferior use. For instance, the use of derricks made of silver instead of wood or steel, or the drilling of two wells when one would be enough to drain efficiently the tract, or the use of high-grade oils to settle dust on roads when low-grade oils would do just as well—are illustrations of economic waste. Physical waste, to the contrary, carries with it the concept of loss without any use whatever. In a sense, all physical waste is economic waste. Obviously, economic waste is not necessarily physical waste. In the early days of proration, many persons, including for a time some of the federal judges, took the position that limitation of production so that it would not exceed the reasonable market demand had to do with economic waste as distinguished from physical waste.[10]

We have already seen that it is now everywhere recognized that production in excess of reasonable market demand inevitably causes physical waste, and several courts have so held, including the Supreme Court

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[10]MacMillan v. Railroad Comm. of Tex., 51 F.(2d) 400 (W.D. Tex. 1931). *Contra:* Cases cited in notes 7 and 8 *supra.*

of the United States, the Supreme Court of Oklahoma, and the Court of Civil Appeals, Third District of Texas.[11]

Frequently, in discussing conservation practices, waste is classified as "physical waste" and "market demand waste." Always the person who undertakes to use the term "market demand waste," as distinguished from "physical waste," has difficulty in explaining the distinction whenever called upon to be precise in his definitions or use of terms. Almost always, when the words "market demand waste" are employed, there is a misunderstanding of the actual facts and practices.

It should also be observed that not a single state statute *prohibits* a regulatory body from considering economic waste, or even from controlling production for the very purpose of preventing economic waste. Indeed, some of the statutes, such as those of Oklahoma and Kansas, specifically provide that the waste which is prohibited shall include economic waste. True it is that the Texas act of 1929, and the Texas act of 1931, provided that the waste which was prohibited should not be construed to mean economic waste; however, the Legislature of Texas in 1932 amended the law by eliminating such language, and the existing statute does not in any way prohibit the consideration of economic factors or even the prevention of economic waste. It may be argued that, as the Texas statute now stands, "waste" means economic waste as well as physical waste.

Obviously, economic conditions and economic factors must be considered by the regulatory agencies in writing their orders as a part of the program to prevent physical waste. There is nothing abnormal in such procedure, and no unwarranted assumption of power.

Moreover, whether or not a statute specifically authorizes or directs the regulatory agency to prevent economic waste apart from physical waste, *no statute authorizes, or probably could legally authorize, regulation which unnecessarily causes economic waste.* Frequently, it is said that the regulatory agency has nothing to do with economic waste, and is not interested in drilling or operating expenses, and deals solely with physical waste. Usually that statement is made when unnecessary wells are under discussion, and the official is seeking to defend a policy which causes the drilling of unnecessary wells, or fails to give a proper share of the allowable for wells already drilled to a density sufficient to drain the lease. This is another instance of loose language, part truth and part foolishness. This much is certain: a regulatory agency cannot

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[11]See cases cited in note 7 *supra.*

legally require unnecessary expenditure as a prerequisite to granting an operator an allowable representing his fair share. For instance, if the operator has drilled enough wells to produce efficiently the oil under a tract, the administrative agency cannot insist that he drill more wells before getting a proper allowable. Such was the holding in the *Rowan* case.[12]

5. Proration

The term "proration," like the other terms discussed herein, is frequently used with varying concepts, and thus it is difficult to understand at times what meaning is intended to be conveyed. For instance, "proration" is frequently used as the antithesis of "rule of capture." Many times it is used as meaning that the production of a state must be limited to the figure estimated by the United States Bureau of Mines to be that which will supply the reasonable market demand for the state. Again, proration is used as synonymous with any regulation under conservation statutes. Frequently, reference is made to proration statutes or proration laws when the reference should be to conservation laws. Confusion often results under these circumstances.

Proration really means a division. For instance, when the top allowable for a field is fixed, the amount is divided or allocated or prorated among the operators in the field, each receiving a pro rata part. Obviously, the division may be made by the use of one or more of a great variety of factors, such as flat well basis, potential, acreage, bottom-hole pressure, sand thickness, or the like. Regardless of the factors which are used, and whether or not the division is a fair one, the allowable production is divided or *prorated* among the operators.

6. Distribution of Allowable to States and Among the Fields and Operators Therein

Considerable interest has been shown in the methods used by state regulatory agencies in determining the top allowable for the state as a whole, and the top allowable for each field in the state, as well as in the method of distributing the field allowable among the operators therein. In the Mid-Continent states which have comprehensive conservation statutes, the capacity production of the wells in each state is much larger than the consumptive demand, making it necessary to limit the amount

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[12]Rowan & Nichols Oil Co. v. Railroad Comm. of Tex., 28 F. Supp. 131 (W.D. Tex. 1939). [The Supreme Court of the United States reversed the trial court and the Circuit Court of Appeals, 310 U. S. 573, 60 Sup. Ct. 1021, 84 L. ed. 1368 (1940), with no discussion of the point under consideration. See discussion in note [15] *infra* and in the concluding remarks to this paper, page 414 *infra*.]

of oil which may be produced. From time to time, usually once a month, public hearings are had as a basis for deciding what regulations and limitations are necessary.

In connection with the fixing of a state allowable, the regulatory agency has before it the past history of production in the state, whether storage is increasing or decreasing nominations of purchasers, and many other factors in addition to the estimates of the United States Bureau of Mines with reference to total consumptive demand for the United States, and the estimated consumptive demand for oil from the state. The estimates or forecasts of the United States Bureau of Mines as to the nation's consumptive demand are based primarily upon the gasoline consumption, which, as stated above, can be estimated with great accuracy. Normally, if enough oil is refined to meet the demands for gasoline, enough by-products are produced to take care of the demand for other commodities made from oil; though the increasing use of furnace oils, and the increasing production of distillates and natural gasoline, may cause further revision of the forecasting technique.

Some difficulty arises in estimating the portion of the total demand which is applicable to each state. The procedure of the United States Bureau of Mines is somewhat complicated, but essentially it is as follows: data are obtained showing changes in storage, movements of oil and products in and out of various districts, including exports and imports. Even if it were possible for me to do so, there is no need to try to explain the entire process used by the Bureau. It has already been detailed by Mr. Breakey, who makes the forecasts.[13] It is sufficient here to say that, basing its action upon past history of movements of oil and products in and out of states, the Bureau apportions the nation's allowable among the states, increasing or decreasing the prior estimate of oil needed from each state, depending upon whether the actual movements show that too much or too little oil was being produced to meet the demand applicable to each state.

It is my understanding that the forecast which is made for each state is really the result of a mathematical calculation based primarily on movements of oil and products, and with no discretion being exercised either to increase or decrease a state's portion because of the existence of facts which might be taken into account if so-called "equity" should be done. It follows, of course, that, should a regulatory agency suddenly increase materially the allowable for that state, and the oil

[13]Record of hearing Nov. 7, 1939, as printed for the use of the Committee on Interstate and Foreign Commerce, pp. 180 *et seq.*

should move freely in commerce instead of going into storage, then such facts would be reflected in reports reaching the United States Bureau of Mines, and in due course the Bureau would increase its estimate of the figure representing that state's share in the market demand for the nation. Obviously, states which are inclined to increase unduly their allowables are likely to obtain some advantage over states which, in the common good, do not try to obtain an unfair share of the markets by similar tactics. Under the present system, there is a tendency for each state to try to increase its share of the national allowable at the expense of other states. In a sense, there is keen competition among the states, thereby reducing the probability of a total limitation to a figure below the normal consumptive demand.

It should be made clear that the states are not bound in any way to follow the forecasts or estimates made by the United States Bureau of Mines. In view of the method which is employed in making the estimates, it is right that some discretion should somewhere be exercised in order to fix the proper allowable for a state, with consideration of all applicable factors. Under the existing system, this discretion is exercised by the regulatory agency. It appears, therefore, that sometimes the allowable for a state is above, and sometimes below, the figure announced by the United States Bureau of Mines; however, on the whole it would appear that, except under rather unusual conditions, the states have fixed allowables quite close to the forecasts of the Bureau.

It has been suggested that the method used by the United States Bureau of Mines should be changed so that the Bureau would include other factors in making its forecasts, such as taking into account whether a state has unfairly increased its allowable in order to get an undue share of the markets, or whether one state is producing a greater share of its reserves than another. It is very doubtful whether such a change would be wise, at least unless rather definite standards are set up to limit the range of the discretion to be exercised. By far the better argument can be made to support the opinion that it is wiser to leave the discretion in the state agencies, continuing the present program.

At any rate, after all facts are considered by a state regulatory agency, it finally reaches its conclusion as to the state allowable and the allowable for each field. Theoretically, perhaps, the state allowable is first determined, and is then allocated among the fields; but, no doubt, more often than not the allowables for fields or areas are first determined, which finally constitute the total allowable for the state. It probably is immaterial whether the start is made at the top or the bottom, for adjustments must necessarily be made. So far, no one has ever worked out any satis-

factory formula for distribution of the state allowable among the fields. The statutes which cover the subject may use different language, but, in the end, about the only standard which has been expressed is that the distribution among the fields shall be on a reasonable basis without discrimination. Obviously, there are hundreds of facts which must be considered in determining whether discrimination exists. It is clear that geographical location of fields, the character of the oil, the nearness to refineries or tidewater, the transportation facilities, and many other facts, properly enter into the amount of production which should be properly allocated to each field or area.

Those who argue that demands or nominations of purchasers in each field should determine the market demand for the field are met with the reply that such a system would unquestionably result in selective buying, making it possible for the purchasers, by nominating high in some fields and low in others, to obtain an undue advantage for themselves or for others, to say nothing of being able, in some instances, to affect materially the price of oil and the values of properties in certain areas or fields. It seems sufficient to repeat that all manner of complications enter into allocation of the state allowable among the fields. The present system, which is in a large sense a mere matter of trial and error, adjustments being made from time to time, has worked fairly well. Sooner or later someone will be smart enough to suggest a better system. No witness in support of federal regulation appears to have done so.

Having fixed an allowable for a field which is less than its total productive capacity, the regulatory body is then faced with the problem of prorating the allowable among the producers. And a real problem it appears to be to one who does not know that many of the complications in which the regulatory agencies find themselves with respect to proration of field allowables are self-induced. Too many of these agencies have been unable to withstand at times the opportunity to exercise broad discretion in a manner to take, by unfair proration, the property of one operator for the benefit of another. Statutory proration formulas, as a cure for these discriminatory actions, would not be successful because of the impossibility of writing one formula which will apply to all conditions. Necessarily, the statutes can do little more than announce reasonableness as a standard. In the footnote,[14] citations to some of the

[14]Quotations from the following statutes given in Part IV, p. 1490, n. 37 of this paper as originally prepared, are omitted. All statutes cited are set out at length in 5 SUMMERS, OIL AND GAS (Perm. ed. 1940). Ark. Laws 1939, Act. 105, § 16B; KAN. GEN. STAT. (1935) § 55-604, *as amended* by Kan. Laws 1939, c. 227, § 3(c); LA. GEN. STAT. ANN. (Dart, Supp. 1937) § 9482.3, *amended* by La. Acts 1940, No. 157, § 8; Mich. Laws 1939, No. 61 § 13; N. M. Laws 1935, c. 72, § 12; MISS. CODE ANN. (Supp. 1938) § 2652(g), Miss. Laws 1936, c. 305, § 1; OKLA. STAT. ANN. (1936) Tit. 52, c. 3, § 87; TEX. CIV. STAT. ANN. (Vernon, 1937) Art. 6049c, § 7.

statutes are given. A great variety of methods has been used in making distribution under these statutes. Sometimes distribution is on a flat per-well basis; sometimes on potential, regardless of drilling density; sometimes 100 per cent on acreage; sometimes on a combination of acreage and potential, or acreage and bottomhole pressure. The list could be made extremely long.

Whatever the statute may provide, and whatever formula the regulatory agency may adopt, it is reasonably clear that one fundamental must be met, otherwise the distribution would not be legal. *Without trying to be over-precise, it may be said that distribution must be such that there will be no reasonably avoidable drainage between competitive properties, which is not offset by counter drainage. Stated differently, if it be assumed that all the operators have drilled up their properties, then the order must be such that each operator will have a reasonable opportunity to produce substantially the amount of oil and gas under his tract, subject always to the reasonable necessities for prevention of waste.*

Clearly, the owner of each tract of land, subject to the necessities of waste prevention, has the right to produce the oil and gas under his land without being required to drill unnecessary wells. This right to drill and produce the oil is a property right guaranteed by both state and national constitutions. The orders of the regulatory agency distributing the allowable production must, therefore, be such as will protect the property rights of the various owners. The rights and privileges which these various owners have must necessarily be adjusted and protected, which is all that is meant when the argument is made that it is a duty of the regulatory agency to adjust and protect the rights, or correlative rights, of the common owners in an oil and gas pool, or the owners of lands in a common source of supply.[15]

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[15]Since the text was written, the Supreme Court of the United States has decided (Hughes, Roberts, and McReynolds dissenting) the following cases: Railroad Comm. of Tex. v. Rowan & Nichols Oil Co., 310 U. S. 573, 60 Sup. Ct. 1021, 84 L. ed. 1368 (1940); *pet. for reh. denied*, 311 U. S. —, 61 Sup. Ct. 66, 85 L. ed. (adv. op.) 72 (1940); Railroad Comm. of Tex. v. Rowan & Nichols Oil Co., 311 U. S. —, 61 Sup. Ct. 343, 85 L. ed. (adv. op.) 321 (1941); and Railroad Comm. of Tex. v. Humble Oil & Refining Co. 311 U. S. —, 61 Sup. Ct. 347, 85 L. ed. (adv. op.) 324 (1941). Few lawyers agree with respect to the precise holding in these cases, though it is probable that the Supreme Court has at least said that where jurisdiction of the federal court is not based on diversity of citizenship, but is based on the claim of the existence of a right under the Federal Constitution, the federal courts should not interfere with regulation by a state administrative agency allocating oil production in a case where procedural due process is shown, unless it appears beyond doubt that there was no basis for the regulation or allocation. Some lawyers argue that the Court held in the cases mentioned that the trial courts did not even have jurisdiction. For two conflicting opinions as to the interpretation of the first opinion in the *Rowan & Nichols* case, see Summers, *Does the Regulation of*

Beyond doubt, many instances could be cited showing that highly discriminatory methods of distribution have been used so that some operators have been permitted to produce more, and others less, than their fair shares. On the other hand, progress has been made in all states with respect to methods of proration. It was a very natural thing that in the beginning the potential factor was given great weight, if not taken as a sole factor, even where there was great disparity in drilling density. Oil men had for years drilled and produced as they pleased, and it was the custom to treat potential as a very definite index of the amount of oil which would be recovered from the well, whether it was on a one-acre tract or a ten-acre tract. When, however, regulatory agencies stepped in and tied the hands of operators so that they could not drill and produce as they pleased, it necessarily followed that the agencies had to protect operators against reasonably avoidable adverse drainage, for the operators were not free to use their own judgment and abilities in an effort to protect their properties.

The advent of conservation and proration brought about intensive scientific studies of oil production, of reservoir contents, and of the behavior of reservoir fluids. Tremendous strides have been made along scientific lines, as will be detailed by others. For instance, the invention of instruments for measuring accurately reservoir pressures was of great value, for obviously oil and gas move from high pressure areas to low pressure areas; consequently, when pressures are known, the direction and degree of movement can be determined with reasonable accuracy. Furthermore, having information as to pressures, the production from wells or areas can be increased or decreased in order to minimize or even

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Oil Production Require the Denial of Due Process and the Equal Protection of the Laws? (1940) 19 TEX. L. REV. 1 and Davis, *Judicial Emasculation of Administrative Action and Oil Proration: Another View* (1940) 19 TEX. L. REV. 29. See also the article by Professor Summers on *The Rowan & Nichols Cases*, page 417 *infra*.

Furthermore, those who are familiar with the facts assert that they are not clearly stated in the opinions, and that actually there was no real conflict in the evidence, and the trial court so held.

At any rate, it is asserted that the opinions do not conflict with what is said in the text of this article, at least on the points under discussion in the text to which this note relates. It may be that federal courts, where jurisdiction is asserted under the claim of denial of due process (not procedural), should refuse to accept jurisdiction, or should not interfere with a state conservation agency unless it be conclusively shown that its act was outrageously confiscatory or arbitrary, but it does not follow that the act of the agency is in accordance with law. Certainly a state court has broader powers than those which seem to have been recognized as proper for a federal court to exercise. It may even be forcibly argued that the federal courts, in a case where jurisdiction is based on diversity of citizenship, would be authorized to interfere if jurisdiction were based solely on the existence of a federal question, such as lack of due process of law under the Fourteenth Amendment. See further discussion in concluding remarks of this paper, page 414 *infra*.

change the direction of migration. Again, the technique of taking cores or samples of the sand, and of measuring with considerable accuracy the sand thickness, saturation, permeability, and other factors—have made it possible to obtain knowledge of underground conditions and to control reservoir reactions following production to a degree which was unheard of in 1930.

All of which is to say that, though many mistakes have been made in the past in allocation of production which resulted in discrimination, and even though many instances of discrimination can still be shown in existing orders, it is fair to remember the great progress which has been made, and it is not unreasonable to think that most of the discrimination which now exists will in time be removed, even if it be necessary for the courts to play their part in preventing continuation of the existing discriminations. Several recent cases, establishing rights of operators and regulatory agencies under the state statutes which were involved, are great aids to conservation, and to a solution of some of the problems which have arisen, especially with respect to unnecessary wells and the distribution of allowable.[16]

Finally, it should be said that a distribution formula proper for one field may be wholly inappropriate in another. The use of one formula for all fields would certainly not bring about the results which ought to be obtained—the prevention of reasonably avoidable drainage between competitive tracts, not offset by counter drainage.

7. Pooling to Prevent Confiscation of Small or Irregularly Shaped Tracts

As we have seen, there is little disagreement among engineers on the point that ratable production should be sought, it having a definite bearing on the efficient operation of a pool. It is also well established that relatively uniform spacing is desirable, if for no other reason than that it simplifies the problem of obtaining ratable production. Some of the statutes specifically direct the administrative agencies to do whatever is reasonably necessary to prevent the drilling of unnecessary wells. These

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[16]Rowan & Nichols Oil Co. v. Railroad Comm. of Tex., 28 F. Supp. 131 (W.D. Tex. 1939), *aff'd*, 107 F.(2d) 70 (C.C.A. 5th, 1939); Croxton v. Corporation Comm. of Okla., 186 Okla. 249, 97 P.(2d) 11 (1939); Patterson v. Stanolind Oil & Gas Co., 182 Okla. 155, 77 P.(2d) 83 (1938), *appeal dismissed*, 305 U. S. 376, 59 Sup. Ct. 259, 83 L. ed. 231 (1939). See note [15] relating to *Rowan & Nichols* cases.

statutes provide for uniform spacing and for drilling or proration units.[17] Such a unit is defined in the Arkansas statute as being

> "the maximum area which may be efficiently and economically drained by one well." [Ark. Laws 1939, Act 105, § 14.]

It seems logical to say that, if it reasonably appear that one well will drain a given area, say 40 acres, the owner of the 40-acre tract with a well thereon ought to get an allowable appropriate for the 40-acre tract, and that his allowable should not be increased should he drill three or four wells on the tract, each being unnecessary. On the other hand, if one well will drain a given area, say 40 acres, then, should an operator have only a 10-acre tract, it seems illogical to require him to drill a well on the 10-acre tract merely to produce an allowable appropriate to the tract, when such well is capable of draining as much as 40 acres. Moreover, it seems illogical and discriminatory to permit such operator to drill a well on a 10-acre tract and have the same allowable as his neighbor with a well on 40 acres. Obviously, tracts which cannot be drilled in conformity with a uniform spacing plan, or in conformity with a program of drilling or proration units, present complications.

For many years, operators, regulatory bodies, and courts were greatly influenced by customs of long standing under which an operator drilled and produced as he pleased, and successfully asserted the right to drill on a small tract or to great density on large tracts, regardless of the fact that he might drain neighboring tracts or cause unnecessary wells to be drilled on neighboring tracts in order to secure protection against undue drainage. It is not surprising that these customs influenced early administration of conservation laws, resulting in many exceptions to well-spacing programs. These exceptions, combined with a proration formula which gave great value to potentials or to mere wells, brought about many discriminations. Gradually, however, progress was made toward taking care of the small or irregularly shaped tract, and toward the elimination of discrimination when unnecessary wells are drilled, with New Mexico making a valuable contribution by its law specifically authorizing compulsory pooling, though the law did have an unfortunate proviso which virtually annulled the compulsory feature. Oklahoma followed with a spacing and pooling law; also Louisiana. Best of all was Arkansas which authorized compulsory pooling, this being an improvement over the New Mexico law, as will be explained.

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[17] *Arkansas:* Ark. Laws 1939, Act 105, § 14. *Louisiana:* La. Acts 1936, No. 225, § 6-(6). *Michigan:* Mich. Acts 1939, No. 61, § 13. *New Mexico:* N. M. Laws 1935, c. 72, § 12. *Oklahoma:* Okla. Acts 1935, c. 59, *amending,* Okla. Acts 1933, c. 131, 4 [La. Acts 1940, No. 157, §§ 8 & 9 supersedes similar provisions of La. Acts 1936, No. 225.]

Let us assume a field in which one well will drain efficiently as much as 40 acres, and that the regulatory agency of New Mexico issues an order providing for spacing of wells on not less than a 40-acre pattern, and also providing for a proration unit of 40 acres. If all operators had 40-acre tracts conforming exactly to the 40-acre unit, then each operator would, in conformity with the regulations, drill approximately in the center of the unit, and there would not be an unnecessary well in the entire field. Distribution of the allowable would be made upon a formula which would prevent reasonably avoidable drainage between competitive units. Such a situation would be close to the ideal. However, let us now assume that, within the limits of a unit, there is a tract of 30 acres and another of 10 acres. Obviously, the uniform pattern would be upset if each of the owners of these two tracts drilled substantially in the center of his tract. Furthermore, there would be at least one unnecessary well, for, under the facts assumed, one well will efficiently drain as much as 40 acres. Let us also assume that each well costs $50,000 to drill, and that the recovery per acre will be 5,000 barrels of oil worth $1.00 a barrel. Under the New Mexico law, should the owners of the two tracts not make a pooling agreement, the Commission would, after a hearing, issue a pooling order. Let it be assumed that the order authorizes one of the operators to drill a well in the center of the 40-acre unit, each operator to pay for the expense of drilling and operating in proportion to the acreage owned, each getting a similar share of the production allowed for the whole unit. Should the operators elect to abide by the Commission's order, all would be well. However, let us next assume that the owner of the 30-acre tract refused to pool, insisting on the right to drill, providing that no waste would take place should he do so. Under the New Mexico statute, a permit to drill would have to be issued to the owner of the 30-acre tract, who would then drill a well at a cost of $50,000. He would get 30/40ths of the amount which would be allowed to the entire 40-acre unit, this being in proportion to the acreage which he owned therein. Let it be assumed that, even though he paid the entire expense of drilling and operating the well, he could still make a profit though limited to an allowable representing 30/40ths of the allowable to the 40-acre unit. In a way, this operator could not claim any confiscation. Let us see, however, what would happen to the owner of the 10-acre tract.

Inasmuch as the owner of the 30-acre tract had refused to pool, the owner of the 10-acre tract would in turn be required to spend $50,000 to drill a well on his 10-acre tract. His share of the allowable production would be 10/40ths of the total allowable for the unit; however, since

the ultimate production from the 10-acre tract would be 5,000 barrels per acre, the ultimate production would be only 50,000 barrels of oil worth $1.00 a barrel; consequently, having spent $50,000 to drill the well, and having received in return over a period of years only $50,000, the owner of the 10-acre tract would actually lose money, represented by operating expenses, interest, taxes and similar expense.

If the New Mexico law were the same as the Arkansas law, then, under the facts assumed, the regulatory agency could have enforced pooling so that only one well would be drilled on the 40 acres. Everybody would be better off than under the situation just outlined. The same amount of oil would be produced from the 40 acres, whether one or two wells were drilled; consequently, the income to the landowners would be the same in either instance. The losers would be the operators, for they drilled an unnecessary well costing $50,000.00, and they doubled necessary operating expense. It is also clear that, under the law as it exists in New Mexico, and under the assumed facts, the owner of the 30-acre tract may have refused to pool because he knew that the owner of the 10-acre tract could not afford to drill if limited to a proper allowable; consequently, the owner of the 30-acre tract would be able to drain eventually the oil from under the 10-acre tract. It follows that the New Mexico statute, instead of protecting, as it was intended to do, the owner of a small tract, may make it possible to bring about confiscation. The Arkansas statute gives the regulatory body the power to *enforce pooling* and thereby prevent unnecessary wells and the confiscation of small tracts. Under Arkansas law, the small tract owner is not at the mercy of the owner of the larger tract.

There is little doubt with respect to the validity of pooling statutes. Cases and articles in support are cited in the footnotes.[18] Furthermore,

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[18]Veasey, *Compulsory Pooling of Adjacent Tracts into Drilling Units to Conform to an Established Well Spacing Plan,* a paper read before the American Bar Association Section of Mineral Law at its Cleveland Meeting, 1938; Walker, *The Problem of the Small Tract Under Spacing Regulations* (1938) 57 TEX. BAR ASS'N PROC. (Oct. TEX. L. REV.) 157, also appearing in (Aug 1, 1938) 37 OIL & GAS J. No. 13, p. 41, (1938) 90 OIL WEEKLY No. 8, p. 22 and also at page 358 of Record of November, 1939, hearings before the Cole Committee of the Interstate and Foreign Commerce Committee of the House of Representatives, printed for the use of the Committee on Interstate and Foreign Commerce; Legal Sub-committee of American Petroleum Institute, *Legal Phases of Well Spacing,* and Engineering Sub-committee of American Petroleum Institute, *Engineering and Economic Phases of Well Spacing* in PROCEEDINGS OF EIGHTH MID-YEAR MEETING AMERICAN PETROLEUM INSTITUTE (1938) Section 1-General, p. 8; See also Tysco Oil Co. v. Railroad Comm. of Tex., 12 F. Supp. 195, 202 (S.D. Tex. 1935); Marrs v. City of Oxford, 24 F.(2d) 541 (D. Kan. 1928), *aff'd,* 32 F.(2d) 134 (C.C.A. 8th, 1929), *cert. denied,* 280 U. S. 573, 50 Sup. Ct. 29, 74 L. ed. 625 (1929); Croxton v. Oklahoma, 186 Okla. 249, 97 P.(2d) 11 (1939); Patterson v. Stanolind Oil & Gas Co., 182 Okla. 155,

unless a statute sets forth the procedure or limits of power to be exercised in connection with pooling, or clearly prohibits pooling, it is likely that the right to require compulsory pooling is implied, being a reasonable method of preventing waste and avoiding confiscation.[19]

8. Unit Operation

The pooling of small or irregularly shaped tracts in order to make effective a uniform spacing program, or to prevent drilling of unnecessary wells, though it be a joint venture as described above, is quite a different type of regulation from that which is meant by the use of the words "unit operations." When the term *unit operations* is used, it is intended to convey the idea of operating an entire field, or at least a large portion thereof, as a unit, or as if owned by one person.

Much has been written about the value of unit operations. It is argued that many of the evils arising from the usual method of operations are obviated under a unit-operation program. It is said, for instance, that the cost of operations will be reduced; the wells will be drilled and operated solely with efficiency of recovery in view; and, consequently, ultimate recovery will be higher under unit operations than if the usual procedure under conservation statutes should be followed, and even though the regulation be of high order. It is probably true that some of the argument is sound. Theoretically, unit operation is ideal, but it is quite another thing to translate that ideal into actual practice.

Unit operations may roughly be divided into two types: (1) voluntary, and (2) compulsory. Voluntary unit operation takes place whenever the interested persons in a field make an agreement so that the entire field or a large part thereof, irrespective of property lines, may be operated as a unit in accordance with the program outlined in the agreement. There are several agreements of this type, notably those with respect to Kettleman Hills, in California, and Van, in Texas.[20] Similar

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77 P.(2d) 83 (1938), *appeal dismissed, per curiam*, 305 U. S. 376, 59 Sup. Ct. 259, 83 L. ed. 231 (1939); Ely, *The Conservation of Oil* (1938) 51 HARV. L. REV. 1209, 1235; German, *Compulsory Unit Operation of Oil Pools* (1931) 17 A.B.A.J. 393, and (1932) 20 CALIF. L. REV. 111; Summers, *Legal Rights Against Drainage of Oil and Gas* (1939) 18 TEX. L. REV. 27.

[19]See articles cited in note 18 *supra*, especially *Legal Phases of Well Spacing*, in PROCEEDINGS OF EIGHTH MID-YEAR MEETING OF AMERICAN PETROLEUM INSTITUTE (1938) Section I-General p. 8 at 11, ¶ 20; and Walker, *The Problem of the Small Tract Under Spacing Regulations* (1938) TEX. BAR ASS'N PROC. (Oct. TEX. L. REV.) 157, 168 and at 362 of Record of November hearings before the Cole Committee, cited in note 18 *supra*.

[20]Lindsley and Dahlgren list a number of pools which have been unitized in some form, at p. 499 of Record of Hearings for November, 1939 before the Cole Committee as printed for use of the Committee on Interstate and Foreign Commerce of the House of Representatives, admitting that the total number is relatively small.

agreements should be encouraged. It is observed, however, that those unit operations have been brought about by voluntary agreements. The interested persons, after the usual give and take which precede a contract, finally decided how the production should be divided, how expenses of drilling and operating are to be paid, and the like.

There are two main reasons why unit-operation agreements are not entered into more frequently. First, there is the extraordinary difficulty of bringing together into an agreement all of the lessors and all of the lessees of a field or pool, particularly since, to be of much value, the agreement must be made very shortly after the field is first discovered and long before it has been definitely outlined and the true value of its properties are ascertained. Second, there is the fear, whether unfounded or not is unimportant, that the state or the federal government will bring an anti-trust suit claiming that the agreement is not primarily for the purpose of operating the field efficiently and cheaply in accordance with the best engineering practices, and in full compliance with the strictest of conservation laws, but, to the contrary, is a scheme to control production or to raise prices.

In some of the states there are laws specifically authorizing the making of unit-operation agreements, which, when approved by some state agency, will protect the parties to the contract against any prosecution under anti-trust or monopoly laws.[21] No doubt, the statutes of all the states ought to contain such a provision; and a similar provision should be passed by the National Congress; however, as pointed out in testimony given in these hearings, regardless of laws specifically authorizing approval of unit-operation agreements, a very limited number have been entered into, and for the good reason that the owners of the oil land, frequently large in number, simply cannot agree upon terms. If they could, no doubt the regulatory agency would be glad to issue a regulation which would follow the unanimous recommendation of the interested persons, subject to necessary changes for waste prevention.

Turning now to compulsory unit operation, very different questions arise. No state has yet passed a law authorizing the regulatory body to *require* unit operations. Texas has even gone so far as to write into its primary conservation act the following clause:

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[21] *Arkansas:* Ark. Laws, Act 105, § 15, ¶ B. *California:* CAL. GEN. LAWS (Deering, 1937) Act 4916, § 8c. *Kansas:* Kan. Laws 1939, S. B. 185, § 3 *Mississippi:* MISS. CODE ANN. (Supp. 1938) c. 166B, Miss. Laws 1932, c. 117, § 40. *New Mexico:* N. M. Laws 1935, c. 72, § 12.

> "However, it is not the intent of this Act to require repressuring of an oil pool or that the separately owned properties in any pool be unitized under one management, control or ownership." [TEX. STAT. (Vernon, 1936) Art. 6014, § g.]

It should be added here that apparently this clause deals solely with unit operations as commonly understood, as distinguished from a regulation providing for the pooling to prevent confiscation of small or irregularly shaped tracts, as discussed above.[22]

It is freely admitted that unit operation of a field is a splendid thing. However, complications arising from compulsory unit operations are considered to be almost insurmountable. As observed above, if unit operation of a field is to be effective, the program should be formulated in the early stages of its history. Obviously, if the field is already drilled up, or substantially so, it is then too late to provide for unit operation. Let us assume, therefore, that several wells have been completed in an area which unquestionably constitutes a new field. Undoubtedly, there is available a reasonable amount of geological and geophysical data, giving some indication of the probable extent of the field. If, at this point, a hearing should be had before a regulatory agency for the purpose of formulating a program for unit operation of the field, whatever its extent and character, the program would have to provide for valuing in some way all properties within the limits found from meagre evidence to be within the productive area, or the program would have to provide some method for taking care of tracts later found to be productive or non-productive, contrary to a previous classification. The program would have to provide money for drilling and operating wells, and for distribution of the allowable production at a time when few facts exist as to the relative values of properties. If exploratory wells should first be drilled, such fact finding procedure might cover a considerable period, and the owners and lessees of the land in the area would be deprived of the right to do their own drilling, and to secure immediate income.

Beyond question, it would be found that changes would have to be made from time to time in the relative values of tracts, frequently

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[22]Walker, *The Problem of the Small Tract Under Spacing Regulations* (1938) TEX. BAR ASS'N PROC. (Oct. TEX. L. REV.) 157, also appearing in (1938) 90 OIL WEEKLY, No. 8, p. 22; (Aug. 1, 1938) 37 OIL & GAS J. No. 13, p. 41 and also at page 358 of the record of November, 1939, hearing before the Cole Committee of the Committee on Interstate and Foreign Commerce, says near the end of the article that the clause quoted in the text merely provides that repressuring or unit operation is not *required,* leaving the Commission free to act, at least with respect to pooling. German, *Compulsory Unit Operation of Oil Pools* (1931) 17 A.B.A.J. 393, (1932) 20 CALIF. L. REV. 111, discusses legal and practical phases of joint operation of fields and wells.

requiring refunds by royalty owners and lessees. The many complications arising from entering an order requiring compulsory unit operations become apparent. The facts would be too meagre to permit findings as to relative values of properties supported by substantial evidence; consequently, it is extremely doubtful whether such an order would stand up in court. The chances are that it would be stricken down as being unreasonable, constituting an unwarranted regulation of property rights.

It cannot be denied that a compulsory unit-operation order would restrict the use of property and the discretion of the owners far more than does the usual type of conservation regulation now current. The ultimate recovery likely under a compulsory unit-operation program, as distinguished from a normal conservation program, would have to be very great before a court would hold that the extraordinary restrictions in the use of property which would take place under the compulsory unit-operation program were justified as a reasonable means of preventing waste and protecting property rights. It is more likely the courts would hold that such restrictions were far beyond the necessities of the case.

This much is certain: the merits of compulsory unit operations, as against reasonably efficient and effective control under existing conservation statutes, are not well enough established to overcome in legislative bodies the reluctance to give administrative agencies far greater powers than are now being exercised. I think it can be said that no compulsory unit operations law would have a chance to pass either in Congress or in any state legislature. Moreover, no regulatory agency is likely, under present state of knowledge, to issue a compulsory unit-operation order without being clearly directed by statute to do so.

II. Probable Defects in Existing State Statutes

A. *Statutes Generally Satisfactory*

On the whole, the existing state statutes are reasonably satisfactory, at least in Arkansas, Kansas, Louisiana, Michigan, New Mexico, Oklahoma, and Texas. By stretching the facts more than is warranted, Mississippi could be included. There is no intention to say that the statutes in these states are perfect, for most of them could be overhauled and revised with much improvement; but it is erroneous to say that they are wholly inadequate, making federal control necessary.

Complaint is frequently made that the statutes of many states give too much power to the regulatory agencies and allow them too much discretion.[23] It has been demonstrated over and over again that the legis-

[23]Testimony of E. O. Thompson, member of the Railroad Commission of Texas, given in the hearing before the sub-committee in New Orleans, Dec. 11, 1939, is to that effect.

lature cannot foresee all problems which are to be disposed of in connection with conservation practices; consequently, it is utterly impossible to write a law which leaves no discretion to the administrative agency. More often than not, when a statute goes into too much detail, the foresight is erroneous, and complications arise which require another act of the legislature to cure. Such a method is not flexible enough to meet changing conditions. It must be admitted, however, that whenever broad general authority is given to a regulatory agency, the opportunity is given for unwise, arbitrary and discriminatory action. For such actions, however, the officials must take the blame, being unable to say that they were simply doing what the statute specifically required. At any rate, the point here to be made is that the existing state statutes are on the whole reasonably satisfactory. A few specific defects will, however, be mentioned.

B. *Compulsory Pooling Should Be Included*

It has already been pointed out that, in order to enforce a uniform well-spacing program, to prevent the drilling of unnecessary wells, and to prevent the confiscation of small or irregularly shaped tracts, it is desirable for the statute to give to the regulatory agency the right to require pooling. There is no need to repeat what has already been said above on that point. While the power doubtless exists by implication, unless its exercise be prohibited, the value of having clear statutory authority is obvious.

C. *Authorize Voluntary Unit Operations*

The probable benefit by the operation of a pool as a unit is well recognized, as we have seen above. Should the state and federal statutes specifically authorize operations under a unit-agreement program, it is likely that more of these agreements would be made. In those states where the agreements are specifically authorized, it is also provided that the approval of some official or agency must be secured. There appears to be no objection to a provision of that character.

D. *Clarify Function of Court in Connection With Judicial Review*

At the very outset of this discussion, it should be made clear that, with the possible exception of Oklahoma which has a peculiar procedure and a peculiar judicial-review program, no state statute makes the administrative agency, with respect to violation of regulations, both prosecutor and judge. The state statutes in substance provide on the whole that, if knowledge of a violation be obtained, request must be made of the Attorney General to sue for injunction or penalty, or both. The court, not the administrative agency, makes the final decision with respect

to the occurrence of the violation and the remedy to be applied if guilt be proved. No doubt, the suit could be defended by asserting invalidity of the statute or regulation.

All of the modern statutes make rather elaborate provision for testing the validity of the conservation statutes or any act of the regulatory agency thereunder, without first violating, and then asserting invalidity in the suit brought by the state for penalty or injunction. The usual statute provides that any interested person who desires to test the validity of the regulatory control is authorized to bring an injunction suit. The statute and the rule, regulation or order complained of are usually declared to be *prima facie* valid, though doubtless *prima facie* validity would be the rule, regardless of statutory declaration. There is no need here to determine whether, under any particular statute, the trial is wholly *de novo,* or whether the transcript of the proceedings before the regulatory agency may be introduced, and for what purposes, or, if introduced, whether it may be supplemented. As far as this discussion is concerned, it will be assumed that adequate right exists to present to the court the facts with respect to the points at issue.

Most of the cases arising under the conservation laws raise the constitutional question of confiscation, and also denial of equal protection of the laws. For instance, an operator brings suit attacking the validity of the allowable fixed for a lease, asserting that the regulatory agency is acting beyond its proper power by fixing an allowable much less than that to which the operator is entitled, with the result that he is not permitted to produce his fair share. It is asserted that such unwarranted taking of property is without due process of law and denies to the operator the equal protection of the laws. What is the proper function of the court in a suit of this character? To simplify the discussion, let it be assumed (and the assumption is justified) that the regulation fixing the allowable, being prospective in nature, is legislative in character, often called quasi-legislative. It seems to be reasonably clear that the making of a conservation regulation, providing a rule of conduct for the future, is not the exercise of a judicial function, though the procedure (notice and hearing) may simulate judicial procedure, and be called, with some justification, quasi-judicial.[24]

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[24]Labels, such as *quasi-judicial* and *quasi-legislative,* have caused some confusion. An administrative board may, as a basis for exercise of a legislative function, adopt, or be required to follow, a procedure which is typical of the exercise of a judicial function; nevertheless, the nature of the action is still legislative, and its validity should be tested as such. See brief discussion of this point by the author hereof, Hardwicke, *Legal History of Conservation of Oil in Texas* in LEGAL HISTORY OF CONSERVATION OF OIL AND GAS, A SYMPOSIUM (1938) 260, n. 55. H. R.

There seems to be considerable confusion in the cases bearing on suits of the general type under discussion, most of them by the Supreme Court of the United States. If the doctrine announced in one line of cases be followed, then the trial court should simply hear the evidence and uphold the distribution order if there be substantial evidence in the record to support it. In other words, according to these cases, the court should take the position that it should not usurp the functions of the regulatory agency by overturning the order and the factual findings if, from the evidence, it appears that reasonable men could have reached the same conclusion as did the regulatory agency. It is argued that on the whole the regulatory agencies are composed of experts, or of men thoroughly familiar with the subject matter; consequently, they are in a better position to weigh the testimony and reach a proper conclusion than is the court which must proceed in the traditional manner. Obviously, the argument supporting this line of decisions is strong. The rule has been stated in several conservation cases, though, curiously enough, it appears that in almost all of them the court did not actually follow the rule as announced, but undertook to decide many of the fact questions.[25]

There is another line of cases supporting the rule that, in a *case involving confiscation and discrimination such as is under discussion,* the court must not only pass on the legal questions, but, in order to perform its duty, *it must also make independent determinations of fact,* not being bound by the findings of the administrative agency, even though supported by substantial evidence, and regardless of the fact that, from the evidence, reasonable men could have reached the same conclusion as did the regulatory agency. These cases say that a person is entitled to a judicial determination of whether his constitutional rights have been denied, and that the judicial function cannot be exercised if the court be denied the right

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7372, offers an illustration: the Commissioner, in promulgating general waste prevention regulations under Section 6 doubtless would perform a legislative function, frequently called quasi-legislative; should he file a complaint asserting violation of the regulation, conduct a hearing, and issue a cease-and-desist order under Section 15, he would perform a judicial function, frequently called quasi-judicial.

[25]Typical cases where courts actually made fact findings: Rowan & Nichols Oil Co. v. Railroad Comm. of Tex., 28 F. Supp. 131 (W.D. Tex. 1939), *aff'd,* 107 F.(2d) 70 (C.C.A. 5th, 1939). [The *Rowan & Nichols* case, *supra,* was reversed in the Supreme Court. See discussion in note [15] *supra* and in concluding remarks to this paper, page 414 *infra.*] Thompson v. Consolidated Gas Util. Co., 14 F. Supp. 318 (W.D. Tex. 1936), *aff'd* 300 U. S. 55, 57 Sup. Ct. 364, 81 L. ed. 270 (1937); Peoples Petroleum Producers v. Smith, 1 F. Supp. 361 (E.D. Tex. 1932); MacMillan v. Railroad Comm. of Tex., 51 F.(2d) 400 (W.D. Tex. 1931).

to make independent determinations of fact. It is clear that this argument is also supported by sound reason.[26]

No good purpose would be served by an exhaustive discussion of the two lines of cases, or a disclosure of what the courts actually do in reaching their decisions, regardless of the viewpoint expressed as to what is the court's proper function. The subject has been discussed in some detail by the writer, beginning at page 261 of the "Legal History of Conservation of Oil and Gas, A Symposium."[27] If it be assumed that the legislature has the right to provide which rule should be followed, it becomes important, then, to determine which is the better rule.

First of all, it may definitely be said that, *regardless of any constitutional question which may be involved,* it appears to be unwise to provide that the findings of fact by the regulatory agency shall be conclusive, whether or not supported by substantial evidence; and it may also be unwise, in cases involving constitutional questions, to limit review of facts to a mere determination of whether substantial evidence upholds the facts supporting the regulation. It must be admitted that, if review should be so limited, the review would tend to become more or less perfunctory, and the opportunity would exist for the regulatory agency to cover up arbitrary and discriminatory action.

Some years ago, Mr. Chief Justice Hughes, in discussing the question whether legislation should go as far as possible to uphold findings of fact by regulatory agencies, made this observation:

> "The power of administrative bodies to make findings of fact which may be treated as conclusive, if there is evidence both ways, is a power of enormous consequence. An unscrupulous administrator might be tempted to say, *'Let me find the facts . . . I care little who lays down the general principles.'* " (Italics added.)[28]

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[26]St. Joseph Stock Yards Co. v. United States, 298 U. S. 38, 56 Sup. Ct. 720, 80 L. ed. 1033 (1936); Ohio Valley Water Co. v. Ben Avon Borough, 253 U. S. 287, 40 Sup. Ct. 527, 64 L. ed. 908 (1920). The Committee on Administrative Agencies and Tribunals in its report to the Section of Judicial Administration of the American Bar Association (1939) 64 A.B.A.REP. 407, 417, states that where constitutional questions of confiscation of property are involved, then judicial review "requires an independent determination by the court upon questions of fact as well as law."

[27]As pointed out in the discussion appearing in note [15] *supra* and in the concluding remarks to this paper, page 414 *infra*, the Supreme Court of the United States, in the *Rowan & Nichols* cases, apparently has greatly restricted the powers of the federal courts, virtually overruling the line of cases cited in note 26, and also established procedure such as was recognized in Thompson v. Consolidated Gas Co., 300 U. S. 55, 57 Sup. Ct. 364, 81 L. ed. 501 (1937). Unfortunately the opinions in the *Rowan & Nichols* cases are not clear.

[28]See Note (1933) 46 HARV. L. REV. 490. [This statement originally appeared in the N. Y. Times, Feb. 13, 1931 at 18.]

The same idea was expressed in the opinion in the case of *St. Joseph Stockyard Co. v. United States,* wherein Mr. Chief Justice Hughes said:

> "Legislative agencies, with varying qualifications, work in a field peculiarly exposed to political demands. Some may be expert and impartial, others subservient. It is not difficult for them to observe requirements of law in giving a hearing and receiving evidence. But to say that their findings of fact may be made conclusive where constitutional rights of liberty and property are involved, although the evidence clearly establishes that the findings are wrong and constitutional rights have been invaded, is to place those rights at the mercy of administrative officials and seriously to impair the security inherent in our judicial safeguards. That prospect, with our multiplication of administrative agencies, is not one to be lightly regarded. It is said that we can retain judicial authority to examine the weight of evidence when the question concerns the right of personal liberty. But, if this be so, it is not because we are privileged to perform our judicial duty in that case and for reasons of convenience to disregard it in others. The principle applies when rights either of person or of property are protected by constitutional restrictions."[29]

On the other hand, it must also be admitted that, theoretically at least, the administrative agencies are composed of men with special training and with a sense of responsibility comparable to that of the judges. Perhaps it is true that courts, with their rather rigid procedure, are not as well equipped as administrative agencies to get at the true facts. Beyond question, instances may be given in conservation cases, as in other cases, where it may fairly be said that the judges did not fully understand the facts. A judge, after a short trial, has a real task in understanding a great mass of highly technical testimony. Nevertheless, it is also true that judges are well trained to understand complicated facts, and they are relatively free from the same type of pressure and influence which may bear upon members of administrative bodies, particularly if they are elected or have political ambitions. No doubt, in most instances where the judges have failed to appreciate the full significance of the evidence, the heavy business of the courts prevented more leisurely trials or more careful studies of the records. If more judges are needed before better decisions can be rendered, then such remedy is preferable to that of decreasing the extent of judicial review by making virtually final the findings of fact by administrative agencies.[30]

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[29]298 U. S. 38, 52, 56 Sup. Ct. 720, 726, 80 L. ed. 1033 (1936).

[30]Hon. Orie L. Phillips, Judge of the United States Circuit Court of Appeals, Tenth Circuit, in discussing the question whether additional federal judges were needed, said: " . . . I would prefer to err on the side of appointing some judges not

It is my own opinion that *statutes should require* that the courts, at least in cases where confiscation is involved, should make independent determinations of fact, not being bound by findings of the administrative agency, even though these findings be supported by substantial evidence. As pointed out above, this duty may exist anyhow. Before long, the point will surely be cleared up by the Supreme Court of the United States.[31]

Likely enough the courts, though required by statute to make independent determinations of fact, would hesitate to upset findings by the regulatory agency, if there should be substantial evidence to support those findings. The danger of arbitrary action on the part of administrative agencies may indeed be greater than the danger of arbitrary action by the courts, and justification doubtless exists for requiring the courts to make independent findings. If more judges are needed, then let us have them if that be necessary to give adequate judicial review.

Concluding Remarks

What is here said in conclusion was not a part of the original paper prepared for the Cole Committee. The issues with respect to court review of administrative orders are far from settled, justifying further discussion. The comments in Note [15], relating to the recent case of *Railroad Comm. of Texas v. Humble Oil & Refining Co.*[32] and the *Rowan & Nichols* cases, are in point. Those cases do not expressly

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wholly needed than to have judges so overcrowded and overworked that they cannot keep abreast of their dockets, dispose of their cases promptly and expeditiously, and give to the decision of every important controversy their best endeavors and their considered judgment." Phillips, *The Courts and American Democracy* (1940) 27 A.B.A.J. 130, 131.

[31]In San Francisco v. Markey Street Ry., 98 F.(2d) 628 (C.C.A. 9th, 1938) the court, without citing or discussing the *St. Joseph* case, followed the substantial evidence rule. The Supreme Court of the United States denied a writ, which may indicate approval of the holding by the Circuit Court of Appeals. However, the obligation to make independent findings was clearly held in National Fertilizer Ass'n v. Bradley, 18 F. Supp. 263, 274 (W.D.S.D. 1936), based squarely upon the *St. Joseph* case, and the decree was affirmed 301 U. S. 178, 57 S. Ct. 748, 81 L. ed. 990 (1937), but with no discussion of the point with respect to the proper function of the court as to fact issues. The Supreme Court of California, in Drummey v. State Board, 87 P.(2d) 848 (Cal. 1939) which involved cancellation of a license. applied the *St. Joseph* case in holding that the court is not bound by findings of an administrative board, though supported by evidence; then later held, in McDonough v. Goodcell, 91 P.(2d) 1035 (Cal. 1939), that the rule was not applicable in a case which involved *refusal* of a board to grant a permit or license, as distinguished from a case *cancelling* a license already granted. The last case mentioned is discussed in (1939) 27 Calif. L. Rev. 738. [Since the text was written the Supreme Court in the *Rowan & Nichols* cases has apparently settled the question, so that legislation is necessary, especially with respect to cases in the federal courts, to be certain of reasonably broad court review. See discussion of such cases in note [15] *supra* and in the concluding remarks to this paper.]

[32]311 U. S. ...., 61 Sup. Ct. 347, 85 L. ed. (adv. op.) 324 (1941).

overrule the case of *Ohio Valley Water Co. v. Ben Avon Borough*[33] or the *St. Joseph* case, or any other case; yet, as observed in Footnote [15], it is difficult, if not impossible, to reconcile the recent oil cases with the *Ben Avon* or *St. Joseph* cases, much less with *Thompson v. Consolidated Gas Company*,[34] which the minority in the *Rowan & Nichols* cases thought was controlling.

From a practical viewpoint, the protection heretofore declared to exist under the Fourteenth Amendment has been greatly minimized with respect to cases filed in the federal courts in which relief is sought from an order of an administrative agency of a state based on the existence of a federal question arising from a claim of a taking of property without due process of law other than procedural; and the same rule may also be applicable to cases where jurisdiction is based on diversity of citizenship.

If, as the recent opinions of the Supreme Court indicate, the federal courts under existing statutes are virtually denied the right or power to enjoin an act of a state administrative agency where procedural due process is shown, it becomes quite important to define as clearly as possible the powers of administrative agencies and to provide for adequate court review in both state and federal courts, to the end that persons affected by the regulation of their property or business may have a fair opportunity to be protected against arbitrary and unreasonable action of administrative agencies, especially where the regulation affects liberty or property rights. It is not yet established, as the Supreme Court in the *Rowan & Nichols* cases seems to say, that the courts lack competence to understand the problems involved in administrative action, even when some of the questions call for technical knowledge. True it may be that a case, such as the *Rowan & Nichols* case, in which there is technical testimony about oil production, calls for more effort on the part of the judges than would be necessary in a case involving liability on a promissory note; but there is nothing to prevent the judges from taking the necessary time to understand the issues involved.

There may be danger that many of us are becoming so obsessed with the idea of speed, thought to be inherent in administrative agencies but not in courts, or with the idea of clearing court dockets, that we are inclined to restrict materially the traditional powers of our courts. Care may well be taken to avoid over-estimating the wisdom and efficiency of administrative agencies, or minimizing the wisdom and efficiency of the courts. The courts, too, have their responsibility in the

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[33] 253 U. S. 287, 40 Sup. Ct. 527, 64 L. ed. 908 (1920), cited note 26 *supra*.
[34] 300 U. S. 55, 57 Sup. Ct. 364, 81 L. ed. 501 (1937).

solution of the problem. There may be some justification for the criticism that many courts, partly from laziness and partly to clear dockets, are inclined to study cases so superficially, or to impose on court review such limitations or such presumptions in favor of administrative action, that court review really becomes a mere formality or a ritual or "a cloak for ratifying administrative error."[35]

It is evident that the regulation of oil production has resulted in a most comprehensive limitation on the use and enjoyment of property when compared with rights at common law. The administrative agencies have, of course, great opportunities to do much good and also to do much evil. It is not at all unlikely that the experiences of the oil industry under conservation statutes will be most persuasive in working out statutory limitations necessary to be placed on the powers of administrative agencies, and in formulating proper court review of orders of these agencies, with respect to regulation of private property or business.[36]

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[35]The quotation is from *Judicial Review of Administrative Determinations, A Summary and Evaluation,* a very instructive paper by John Dickinson, prepared for the Institute of Administrative Law and Procedure held during the annual meeting of the American Bar Association in Philadelphia, 1940.

[36]A legal committee appointed by the Chairman of the Interstate Oil Compact Commission drafted provisions thought to be suitable for a comprehensive bill for the conservation of oil and gas. The Committee made its report at the meeting of the Compact Commission in Oklahoma City on December 30, 1940. Copies of that draft or bill may be had by writing to the Secretary of the Interstate Oil Compact Commission, Oklahoma City, Oklahoma. In several instances, alternative sections were prepared. This was done with respect to court review. One draft relates to court review based on the record made at the hearing before the Commission, and contains rather severe limitations on the powers of the courts; the other, or alternative section (No. 12), provides for trial *de novo,* and undertakes to give the courts greater freedom and powers, especially where allocation of production is concerned. The author of this article favors the last mentioned draft of Section 12 of the Compact Bill.

The Compact Bill represents the present stage of the evolution of conservation legislation. The growth may be observed by starting with the New Mexico Act of 1935, c. 72 (the first comprehensive act of the present phase), then studying in turn Okla. Laws 1935, p. 239 (well-spacing act); La. Acts 1936, No. 225; Ark. Laws 1939, Act 105; Mich. Laws 1939, No. 61; and finally La. Acts 1940, No. 157. A large part of the latter act appears in the Compact Bill.

THE ROWAN & NICHOLS CASES

*W. L. Summers**

In 1938 the Texas Railroad Commission issued an order limiting the total daily allowable oil production of the East Texas field to 522,000 barrels and prorating this daily allowable among the producers on a well potential basis. As actually enforced by the commission this order apportioned 98% of the daily allowable of the field among the producers on a *per well* basis. The enforcement of this order, as it applied to the lease of the Rowan & Nichols Oil Company, was enjoined by the District Court[1] on the ground that it was arbitrary and unreasonable and violative of the Fourteenth Amendment and the Texas statute requiring that proration be made on a "reasonable basis."[2] With slight modification, this decree was affirmed by the Circuit Court of Appeals,[3] but it was reversed by the Supreme Court.[4]

In 1939, pending the final determination of the validity of its previous order, the Railroad Commission issued another order fixing the daily allowable of the field at 691,000 barrels and prorating the allowable production among the producers under a plan wherein the factors of well potential, bottom-hole pressure, acreage and sand thickness were given consideration, but only after all marginal wells were allowed to produce to their full capacity, and all non-marginal wells were given a base allowable of 20 barrels per day. The effect of the order, as applied, was that 75% of the field allowable was prorated on a *per well* basis. At the suits of the Rowan & Nichols Oil Company, Humble Oil & Refining Company, and others, the enforcement of this order of the Commission was enjoined by a three judge court as violative of the Texas statute and the Fourteenth Amendment.[5] On appeal, the Supreme

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[1]Rowan & Nichols Oil Co. v. Railroad Comm. of Tex., 28 F. Supp. 131 (W. D. Tex. 1939).

[2]TEX. ANN. CIV. STAT. (Vernon, 1937) Art. 6049c, § 7.

[3]Railroad Comm. of Tex. v. Rowan & Nichols Oil Co., 107 F.(2d) 70 (C.C.A. 5th, 1939).

[4]Railroad Comm. of Tex. v. Rowan & Nichols Oil Co., 310 U. S. 573, 60 Sup. Ct. 1021, 84 L. ed. 1368 (1940), *opinion amended,* 311 U. S. ....., 61 Sup. Ct. 66, 85 L. ed. (adv. op.) 72 (1940).

[5]"The question under the two seems to be approximately the same. If the proration is unreasonable, the statute doesn't give the commission authority to make it. If it is so unreasonable as to be arbitrary, the Constitution does not permit it to be done either by the Legislature or the Commission." Humble Oil & Refining Co. v. Railroad Comm. of Tex., Fischer v. Smith, Rowan & Nichols Oil Co. v. Railroad Comm. of Tex., 35 F. Supp. 573, 574 (W. D. Tex. 1940).

Court vacated the decree and remanded the case for dismissal of the complaint.[6]

The opinion of the Supreme Court in the first *Rowan & Nichols* case came as a distinct surprise to Texas lawyers and to the oil and gas industry. This was only natural, because in a number of previous decisions by the federal courts in Texas, *per well* proration orders had been held arbitrary and confiscatory because they were found to bear no reasonable relation to the prevention of waste or the protection of lease owners' rights against preventable and noncompensated drainage.[7] In these and other decisions of the lower federal courts[8] in which an order of the Commission had been challenged as arbitrary and confiscatory under the statute or the Fourteenth Amendment the judges had disclaimed any authority to substitute their own judgments on matters of legislative or administrative policy for that of the Commission and had emphatically stated that their only duty was to determine from the proof whether an order of the Commission was without a rational basis. These same principles had been applied in reviewing a gas proration order of the Commission in *Thompson v. Consolidated Gas Utilities Corp.*[9] wherein Mr. Justice Brandeis wrote the opinion for a unanimous Court.

Many lawyers could not understand why the decree of the lower court had been reversed. In a dissenting opinion by Mr. Justice Roberts, concurred in by Chief Justice Hughes and Mr. Justice McReynolds, it was suggested that the Court had abdicated its jurisdiction to test the Commission's order because of the technical difficulties of the problem. If the Court had intended to hold that regulations or orders of a state administrative agency may no longer be challenged in the federal courts as arbitrary and confiscatory under the Fourteenth Amendment, it could have so stated in one simple sentence. No such statement appears in the opinion.

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[6]Railroad Comm. of Tex. v. Rowan & Nichols Oil Co., 311 U. S. ——, 61 Sup. Ct., 343, 85 L. ed. (adv. op.) 321 (1941); Railroad Comm. of Tex. v. Humble Oil & Refining Co., 311 U. S. ——, 61 Sup. Ct. 347, 85 L. ed. (adv. op.) 324 (1941).

[7]People's Petroleum Producers v. Sterling, 60 F.(2d) 1041 (E. D. Tex. 1932); People's Petroleum Producers v. Smith, 1 F. Supp. 361 (E. D. Tex. 1932); People's Petroleum Producers v. Smith (E. D. Tex., Tyler Div.) No. 386 in Equity (unreported); Rowan & Nichols Oil Co. v. Terrell (E. D. Tex., Tyler Div.) No. 479 in Equity (unreported).

[8]Consolidated Gas Utilities Corp. v. Thompson, 14 F. Supp. 318 (W. D. Tex. 1936); Henderson Co. v. Thompson, 12 F. Supp. 519 (W. D. Tex. 1935); Texas Panhandle Gas Co. v. Thompson, 12 F. Supp. 462 (W. D. Tex. 1935); Clymore Production Co. v. Thompson, 11 F. Supp. 791 (W. D. Tex. 1935); Amazon Petroleum Corp. v. Railroad Comm. of Tex., 5 F. Supp. 633 (E. D. Tex. 1934); Danciger Oil & Refining Co. v. Smith, 4 F. Supp. 236 (N. D. Tex. 1933); MacMillan v. Railroad Comm. of Tex., 51 F.(2d) 400 (W. D. Tex. 1931).

[9]300 U. S. 55, 57 Sup. Ct. 364, 81 L. ed. 510 (1937).

In a discussion of the first *Rowan & Nichols* case before the Section of Mineral Law of the American Bar Association[10] the writer assumed that the Court had not intended to abdicate its jurisdiction to review the order of the Commission. This assumption seemed amply justified by the language of the opinion and the citation of authority to the effect that where a state acts within its regulatory power in such matters as the conservation of natural resources, the evolution of production and proration formulas belongs to the administrative agency, and where such formulas are challenged in the federal courts as arbitrary and confiscatory, the only function of the court is to determine whether the administrative formula is "without a rational basis."[11] Further justification for this assumption was found in the fact that the Court actually reviewed the record, and seemed to hold that under all of the complicated circumstances disclosed thereby, the Commission's flat *per well* order "was not an unnatural answer to the problem" and that the lower court, despite its disavowal of the fact, had substituted its "notions of expediency and fairness" for those of the Commission. The writer criticized the Court's justification of the *per well* order because it seemed to be based upon: (a) a misinterpretation of the Texas Marginal Well Statute[12] to the effect that the Commission was precluded from fixing the daily allowable of 19,632 wells below 20 barrels, (b) improper inferences from the operation of the Commission's spacing rule to the effect that it was precluded by some state policy or statute from applying the well potential formula to wells on small tracts, (c) a complete disregard of Texas lease and landowners' rights against preventable and noncompensated drainage of oil from their lands as recognized by statute, judicial decisions and the orders of the Commission in granting exceptions to its spacing rule, (d) an assumption that the Commissioners are experts in petroleum geology and engineering, (e) a conclusion from an examination of the records that there was great conflict in the testimony of expert witnesses relative to pertinent physical characteristics of the producing formation, and (f) a lack of scientific knowledge on the part of the trial court. The writer contended that a proper interpretation of the law and the facts as disclosed by the record would have revealed that the *per well* order of the Commission was "without a rational basis" and was arbitrary, because it bore no reasonable

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[10]Summers, *Does the Regulation of Oil Production Require the Denial of Due Process and the Equal Protection of the Laws?* (1940) 19 Tex. L. Rev. 1. See also booklet published by the Section of Mineral Law, American Bar Association (1940).

[11]Summers, *Does the Regulation of Oil Production Require the Denial of Due Process and the Equal Protection of the Laws?* (1940) 19 Tex. L. Rev. 1, 6, 7.

[12]Tex. Ann. Civ. Stat. (Vernon, 1937) Art. 6049b.

relation to the prevention of waste or the protection of correlative rights of lease owners against drainage, and observed that under a review of the record such as that made by the Supreme Court "the taking of private property without due process has become an administrative and not a judicial question."[13]

After the Supreme Court had amended its opinion in the first *Rowan & Nichols* case,[14] Professor Kenneth C. Davis published an interesting article[15] analyzing the opinion and arguing for ultimate administrative finality in the promulgation of oil proration orders. In his analysis of the opinion to determine what the Court had actually held respecting the matter of judicial review by the federal courts of oil proration orders by a state administrative agency, Professor Davis was somewhat perplexed by the fact that the Court, by certain language of the opinion, seemed to deny the lower courts jurisdiction to pass upon the reasonableness or fairness of the Commission's *per well* order and then proceeded to justify the order as a reasonable one. But reconciling this apparent inconsistency on the part of the Court on the ground that the "concept of reasonableness is variable," he concluded that:

> "The Court does abdicate, but the abdication is only partial,' not complete. The Fourteenth Amendment in this type of case still has some vitality. The Court has closed the door to a challenge under that Amendment, but it has kept its foot in the door and retains the power to open the door."[16]

Any comparison of the soundness of the conclusions reached by Professor Davis and the writer as to what the Court held in the first *Rowan & Nichols* case must be made in the light of the Court's own explanation of that holding. Perhaps sensing that its opinion in the first case had not made clear the reasons for its reversal of the lower court's decree, referring to this opinion in the second case, the Court said:

> "This adjustment by the state's expert agency of what in our former opinion we called 'as thorny a problem as has challenged the ingenuity and wisdom of the Legislatures' was attacked on two grounds. It was claimed that an hourly potential formula

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[13]Because of the language in quotation marks, Professor Kenneth C. Davis in *Judicial Emasculation of Administrative Action and Oil Proration* (1904) 19 TEX. L. REV. 29, in footnote 6, assumes that I contended that the Supreme Court did and did not abrogate its jurisdiction to review proration orders. I intended only to say that if future reviews are to be conducted as the Supreme Court conducted the one in the *Rowan & Nichols* case it might as well have openly abrogated its jurisdiction to review. But on the matter of inconsistency on this question I suggest that Professor Davis consult his own discussion at pages 31 to 33.

[14]311 U. S. ___, 61 Sup. Ct. 66, 85 L. ed. (adv. op.) 72 (1940).

[15]Davis, *Judicial Emasculation of Administrative Action and Oil Proration* (1940) 19 TEX. L. REV. 29.

[16]*Id.* at 31. Does the Court abdicate?

> fatally omitted other relevant factors, especially acre-feet of sand. Further it was urged that the minimum allowance of 20 barrels, which nearly absorbed the total production, constituted an illegitimate discrimination against high-producing and thinly drilled areas. We rejected these arguments as an attempt to substitute a judicial judgment for the expert process invented by a state in a field so peculiarly dependent on specialized judgment. We said in effect that the basis of present knowledge touching proration was so uncertain and developing, that sounder foundations are only to be achieved through the fruitful empiricism of a continuous administrative process. Further, that ought not be stifled by drawing from the generalities of the Constitution allegiance to one as against the other speculative assumption even though delusively clothed in formal findings of fact."

This statement, together with other language of the opinion justifying the 1939 proration order, indicates that in neither the first nor second opinion is the Court willing to go quite so far as to say that federal courts may no longer enjoin proration orders because they find them arbitrary or without a rational basis. It is clearly apparent, however, that the Court is declaring a policy to the effect that where a state is acting within its regulatory powers through an administrative agency of its creation, and such acts are challenged in the federal courts as being violative of substantive due process, the presumption of reasonableness of such acts will be considered almost, if not quite, irrebuttable.

In the application of this policy to the review of oil proration orders the Court properly assumes that the formulation of an order limiting the production of an oil field and prorating the allowable of the field among the producers on a reasonable basis requires knowledge of the social and physical sciences. But the Court seems to labor under the mistaken impression that the Texas Railroad Commission is composed of a group of specialists in petroleum geology and engineering, selected by the state because of their extraordinary qualifications, who formulate proration orders on the basis of their own expert knowledge of the producing formation. From these assumptions the Court reasons that where this Commission of experts has formulated a proration order for such a producing formation as that in the East Texas Field, where the problem is further complicated by the Marginal Well Statute and the operation of the Commission's spacing rule, the "Due Process Clause does not require the feel of the expert to be supplanted by an independent view of judges on the conflicting testimony and the prophesies and impressions of expert witnesses."[17]

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[17]Railroad Comm. of Tex. v. Rowan & Nichols Oil Co., 311 U. S. ....., 61 Sup. Ct. 343, 85 L. ed. (adv. op.) 321 (1941).

The reasons set out by Professor Davis in support of his contention that the problems of oil conservation must ultimately be solved through complete administrative finality rather closely parallel the reasons advanced by the Court in support of the proration orders in the *Rowan & Nichols* cases. Like the Court, he insists that the administrative process is so well adapted to the formulation of proration orders and the judicial process is so poorly equipped to solve the problems involved that the time is ripe to stop "judicial emasculation" of the orders of the Commission, particularly by the federal judges. To prove this contention, Professor Davis points to the history of oil prorations in the East Texas Field, the behavior of the judges in their review of proration orders, including the *Rowan & Nichols* cases, and indicts them on numerous counts[18] for their lack of qualification to pass upon the reasonableness of proration orders.

These concurring theories of the Court and Professor Davis and the arguments supporting them relative to the superiority of the administrative over the judicial process in the formation of reasonable proration orders might be more convincing if they bore some relation to the facts when applied to the situation in Texas. The Railroad Commission of Texas is not a body of men selected to administer the conservation laws of the state because of their expert knowledge of petroleum geology and engineering and who act in the formulation of proration orders on the basis of such expert knowledge. The office of railroad commissioner is an elective one. The statute fixes no qualification for the office except that a commissioner must be 25 years of age, a citizen resident of the state, hold no other office and not be financially interested in any railroad campany.[19] The commission is authorized to employ experts,[20] but it does not or should not formulate its proration orders solely upon the advice of these experts. The statute[21] requires that orders of the Commission be issued only after a public hearing. At such hearing any interested party may be heard or produce expert testimony relative to the physical facts of the producing formation. Presumably at least, the Commission formulates its orders on the basis of the testimony presented at the hearing. Review by a court to determine the reasonableness of an order of the Commission is a *de novo* proceeding.[22] It is difficult to

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[18]Davis, *Judicial Emasculation of Administrative Action and Oil Proration* (1940) 19 TEX. LAW REV. 29, 44.

[19]TEX. ANN. CIV. STAT. (Vernon, 1937) Art. 6447.

[20]TEX. ANN. CIV. STAT. (Vernon, 1937) Art. 6030

[21]TEX. ANN. CIV. STAT. (Vernon, 1937) Art. 6049c, § 7.

[22]TEX. ANN. CIV. STAT. (Vernon, 1937) Art. 6049c, § 8; Stanolind Oil & Gas Co. v. Midas Oil Co., 123 S.W.(2d) 911 (Tex. Civ. App. 1938), *writ of error dismissed;* Railroad Comm. of Tex. v. Magnolia Petroleum Co., 130 Tex. 484, 109 S.W.(2d) 167 (1937).

conceive of a hearing before the Commission, or before a court on review, wherein there would not be conflicting evidence of expert witnesses as to various facts relative to the producing formation. The Commission is required to weigh these conflicting opinions of the expert witnesses in the formulation of a proration order. On judicial review of an order, the judges, most of whom have considerable knowledge of the physical facts of the producing formation acquired through the trial of similar cases, must also weigh the conflicting expert testimony and pass upon the reasonableness of the order. The theory that the Commission is better equipped to determine the reasonableness of a proration order is entirely fallacious. Where the reasonableness of a proration order turns upon a proper adjustment between various scientific factors such as well potential, acreage, sand thickness and porosity, bottomhole pressure and water drive, which most courts and scientific experts agree must be taken into consideration in the formulation of a fair order, neither the Commission as presently constituted, nor the courts, may possess all the scientific knowledge necessary to make such adjustment, but must alike rely on the testimony of the experts. But since the order in the first *Rowan & Nichols* case ignored all of these factors as to 98% of the allowable production, the judges needed little or no scientific knowledge to pass upon its reasonableness.

From the history of oil proration in the East Texas Field, Professor Davis reaches the conclusion that if it had not been for the interference by the federal judges "the Commission's sense of justice would in time have become as reliable and as respected as that of the judges, and the expertness of the Commission's staff of specialists could really have been brought to bear upon the difficult problems of proration and well-spacing." If the Commission's sense of justice is not respected and if its staff of experts has not applied its learning to the problems of proration and well-spacing, the blame cannot be attributed to the federal courts. It is true that when oil proration was in the experimental stage, the federal courts held some orders of the Commission invalid because they considered the Commission had exceeded its powers.[23] In the *Peoples* cases in 1933, the Federal Court[24] held *per well* proration orders arbitrary and confiscatory. But after that, until it held the *per well* order in the *Rowan & Nichols* case arbitrary and confiscatory, the Federal Court consistently upheld the Commission's oil proration orders in a number of cases.[25]

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[23]See 1 SUMMERS, OIL & GAS (Perm. ed. 1938) § 96.

[24]See cases cited *supra* note 7.

[25]Amazon Petroleum Corp. v. Railroad Comm. of Tex., 5 F. Supp. 633 (E. D. Tex. 1934); Boxrollium Co. v. Smith, 4 F. Supp. 624 (S. D. Tex. 1933); Danciger Oil & Refining Co. v. Smith, 4 F. Supp. 236 (N. D. Tex. 1933).

One of Professor Davis' most serious charges against the behavior of the federal judges in proration cases is that they "emphasize property rights at the expense of jeopardizing legislative policies." Such an accusation might well have been made against the Commission, for it has granted hundreds of permits to drill wells as exceptions to its spacing rule to prevent "the confiscation of property." Professor Davis emphatically asserts, however, that the only property a landowner in Texas has in the oil under his land for production purposes is that which the Commission, by valid order, permits him to produce.[26] If this statement is true, there can be no contention that a proration order is confiscatory, for the simple reason that the landowner has no property to be confiscated until after the issuance of the order and the goal of administrative finality has been reached. Professor Davis does not seem to realize that through legislative and administrative acts and through a long line of decisions by both state and federal courts it has been established in Texas that landowners have correlative right-duty relations against non-compensated and preventable drainage of oil from beneath their lands and that these legal relations constitute property. Nor does he seem to understand, or at least does not admit, that while the Legislature has authorized the Commission to limit the production of an oil field for the prevention of waste out of regard for the public interest, it also requires the Commission to prorate the allowable of the field on a "reasonable basis" to protect the landowners' property interests. It was, of course, these same property interests which the Supreme Court seemed to ignore in upholding the *per well* orders of the Commission in the *Rowan & Nichols* cases.

In denying a petition for rehearing in the first *Rowan & Nichols* case[27] and again in its opinion in the second case[28] the Court held that the federal courts have no jurisdiction to pass upon the reasonableness of a proration order of the Commission as a violation of the Texas statute requiring proration to be made on a "reasonable basis." The problems which this holding raises are admirably set forth by Professor Davis,[29] and it would be useless to speculate further on them here.

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[26]Davis, *Judicial Emasculation of Administrative Action and Oil Proration* (1940) 19 TEX. L. REV. 29, 47. *"The present law of Texas for production purposes is that each owner may produce, not the oil in place under his land, not as much oil as he can capture, but as much oil, as any valid order of the commission allows him to produce."*

[27]311 U. S. ....., 61 Sup. Ct. 66, 85 L. ed. (adv. op.) 72 (1940).

[28]311 U. S. ....., 61 Sup. Ct. 343, 346, 85 L. ed. (adv. op.) 321 (1941).

[29]Davis, *Judicial Emasculation of Administrative Action and Oil Proration* (1940) 19 TEX. L. REV. 29, 34.

After all, it seems to make little or no practical difference to lease owners whether the Supreme Court has completely abrogated the jurisdiction of the federal courts to review proration orders upon the charge that they violate the Due Process Clause or has retained some scintilla of that jurisdiction to be exercised when the proper situation arises. As long as the Court adheres to the policy announced in the *Rowan & Nichols* cases there seems to be not the slightest chance of a litigant securing the affirmance of a decree of a lower federal court enjoining a proration order on the ground that it violates the Fourteenth Amendment or the state statute. Federal judges are not likely to be selected because of their expert knowledge of petroleum engineering and geology. Experts testifying before these judges on a judicial review of proration orders are not likely to be in complete agreement on all matters pertaining to the physical facts of the producing formation. So if a trial court should enjoin the enforcement of a proration order as arbitrary, the Supreme Court would no doubt reverse the decision on the ground that the "Due Process Clause does not require the feel of the expert to be supplanted by an independent view of the judges on the conflicting testimony and prophesies and impressions of expert witnesses" and console the disillusioned litigant by telling that "The real answer to any claims of inequity or to any need of adjustment to shifting circumstances is the continuing supervisory power of the expert commission." Of course, if the Commission should close all the wells in the field except those of some producing company and place no limit on the production of its wells, the Court's sense of justice might be sufficiently outraged to permit the "feel of the expert to be supplanted by an independent view of the judges."

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NOTES AND COMMENTS

Property Rights in Oil and Gas in Mississippi

The exact nature of the property interests in oil and gas in place is a question of fundamental importance, and one upon which the decisions of the various jurisdictions have not been uniform. The theory which any particular jurisdiction adopts concerning the ownership of oil and gas in place and the nature of property interests created by an oil and gas lease materially influences the determination of numerous important questions which arise in regard to the legal rights of landowners and lessees. The purpose of the present discussion is to analyze the few decisions in which the Mississippi court has dealt with property rights in oil and gas, and to discuss the implications found therein, in an attempt to ascertain which of the various theories the Mississippi court has adopted; and then to discuss the effect which such theory may have upon the decision of a few important questions which are likely to arise in regard to rights of various claimants to oil and gas in place.

The Nature of the Landowner's Interest

Oil and gas, while generally regarded as minerals,[1] are species of property peculiar unto themselves. When the courts were first called upon to decide questions involving oil and gas, they frequently sought by analogy to compare these minerals to other types of property, such as animals *ferae naturae*,[2] subterranean waters,[3] and solid minerals.[4] However, since the scientific information now available has shown that the physical characteristics of oil and gas in place are unlike those of any other form of property, most of the modern courts have discarded such analogies, and have adapted their decisions in recognition of the peculiarities of these particular minerals. The numerous decisions that relied upon such analogies have been a prolific source of discussion.[5]

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[1]Burke v. Southern Pac. R.R., 234 U. S. 669, 34 Sup. Ct. 907, 58 L. ed. 1527 (1913); Skeen v. Lynch, 48 F.(2d) 1044 (C.C.A. 10th, 1931); Crain v. Pure Oil Co., 25 F.(2d) 824 (C.C.A. 8th, 1928); Chino Land & Water Co. v. Hamaker, 39 Cal. App. 274, 178 Pac. 738 (1918); Warner v. Patton, 19 S.W.(2d) 111 (Tex. Civ. App. 1929); Texas Co. v. Daugherty, 107 Tex. 226, 176 S.W. 717, L.R.A. 1917F 989 (1915); Norman v. Lewis, 100 W. Va. 429, 130 S.E. 913 (1926); 1 Summers, Oil and Gas (Perm. ed. 1938) 232, § 135, n. 30; Note (1922) 17 A.L.R. 162.

[2]State v. Ohio Oil Co., 150 Ind. 21, 49 N.E. 809, 47 L.R.A. 627 (1898); Westmoreland & Cambria Nat. Gas Co. v. DeWitt, 130 Pa. 235, 18 Atl. 724, 5 L.R.A. 731 (1889); Medina Oil Development Co. v. Murphy, 233 S.W. 333 (Tex. Civ. App. 1921).

[3]People's Gas Co. v. Tyner, 131 Ind. 277, 31 N.E. 59 (1892).

[4]Hague v. Wheeler, 157 Pa. 324, 27 Atl. 714, 22 L.R.A. 141 (1893); Stoughton's Appeal, 88 Pa. 198 (1879); Note (1924) 29 A.L.R. 586; Veazey, *The Law of Oil and Gas* (1919) 18 Mich. L. Rev. 445, 452.

[5]See, *e.g.*, Ohio Oil Co. v. Indiana, 177 U. S. 190, 20 Sup. Ct. 576, 44 L. ed. 729 (1900); Manufacturers' Gas & Oil Co. v. Indiana Nat. Gas & Oil Co., 155 Ind. 461, 57 N.E. 912, 50 L.R.A. 768 (1900); 1 Summers, Oil and Gas (Perm. ed. 1938) c. 2; Greer, *Ownership of Oil and Gas in Place* (1922) 1 Tex. L. Rev. 162, reprinted in (1923) 29 W. Va. L. Q. 172; Summers, *Property in Oil and Gas* (1919) 29 Yale L. J. 174; Veazey, *The Law of Oil and Gas* (1919) 18 Mich.

Most of the early decisions reflect the court's concern for the migratory nature of oil and gas.[6] This characteristic has been greatly overemphasized, however, because oil and gas in place in the earth are no longer regarded as freely migratory or fugacious.[7] In their natural state, oil and gas are effectively confined within a subsurface structural trap and are in a static condition until tapped by a well. But as soon as a well penetrates the reservoir, a low pressure area is created, and the higher pressure in other parts of the reservoir forces the oil and gas toward the opening. In the course of this migration, the oil and gas frequently transgress property lines. All courts, however, have recognized the impracticability of granting relief to a landowner solely because his neighbor's well has drained, or is draining, oil or gas from under his land.[8] Because of this non-liability for drainage, often called the "Rule of Capture," a number of jurisdictions have concluded that a landowner does not have absolute ownership of the oil and gas beneath his land, but has merely

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L. Rev. 445; Walker, *Fee Simple Ownership of Oil and Gas in Texas* (1928) 6 Tex. L. Rev. 125.

[6]Logan Nat. Gas & Fuel Co. v. Great So. Gas & Oil Co., 125 Fed. 623 (1903); Frost-Johnson Lmbr. Co. v. Salling's Heirs, 150 La. 756, 91 So. 207 (1922); Kelley v. Ohio Oil Co., 57 Ohio St. 317, 49 N.E. 399, 39 L.R.A. 765 (1897); Rich v. Doneghey, 71 Okla. 204, 177 Pac. 83, 3 A.L.R. 352 (1918); Barnard v. Monongahela Nat. Gas Co., 216 Pa. 362, 65 Atl. 801 (1907); Wettengel v. Gormley, 160 Pa. 559, 28 Atl. 934 (1894); Hague v. Wheeler, 157 Pa. 324, 27 Atl. 714, 22 L.R.A. 141 (1893); Westmoreland & Cambria Nat. Gas Co. v. DeWitt, 130 Pa. 142, 18 Atl. 724, 5 L.R.A. 731 (1889); Brown v. Vandergrift, 80 Pa. 142 (1875); Texas Pacific Coal & Oil Co. v. Cormanche Duke Oil Co., 274 S.W. 193 (Tex. Civ. App. 1925); Grubb v. McAfee, 109 Tex. 527, 212 S.W. 464 (1919).

[7]Hardwicke, Innocent Purchaser of Oil and Gas Lease (1921) 7; Miller, The Function of Natural Gas in the Production of Oil (1929) 18; 1 Summers, Oil and Gas (Perm. ed. 1938) c. 1, and c. 4, § 63; Blake, *The Oil and Gas Lease* (1940) 13 So. Calif. L. Rev. 304, 305; Hardwicke, *The Rule of Capture and Its Implications as Applied to Oil and Gas* (1935) 13 Tex. L. Rev. 391; Report vi of the Federal Oil Conservation Board (1930) p. 20.

[8]United Carbon Co. v. Campbellsville Gas Co., 230 Ky. 275, 18 S.E.(2d) 1110 (1929); Higgins Oil & Fuel Co. v. Guaranty Oil Co., 145 La. 233, 82 So. 206, 5 A.L.R. 411 (1919); Kelley v. Ohio Oil Co., 57 Ohio St. 317, 49 N.E. 399, 39 L.R.A. 765 (1897); Barnard v. Monongahela Gas Co., 216 Pa. 362, 65 Atl. 801 (1907); Westmoreland Nat. Gas Co. v. DeWitt, 130 Pa. 235, 18 Atl. 724, 5 L.R.A. 731 (1889); Hunt v. State, 48 S.W.(2d) 466 (Tex. Civ. App. 1932); Hardwicke, *The Rule of Capture and Its Implications as Applied to Oil and Gas* (1935) 13 Tex. L. Rev. 391.

In conducting drilling operations on his land, however, a landowner is under a duty not to injure the common reservoir in violation of the rights of other owners therein. Ohio Oil Co. v. Indiana, 177 U.S. 190, 20 Sup. Ct. 576, 44 L. ed. 729 (1900); Manufacturers' Gas & Oil Co. v. Indiana Nat. Gas & Oil Co., 155 Ind. 461, 57 N.E. 912, 50 L.R.A. 768 (1900); Louisville Gas Co. v. Kentucky Heating Co., 117 Ky. 71, 77 S.W. 368, 70 L.R.A. 558 (1903); Higgins Oil & Fuel Co. v. Guaranty Oil Co., 145 La. 233, 82 So. 206, 5 A.L.R. 411 (1919). The courts have clearly recognized this in sustaining the constitutionality of modern conservation legislation.

the exclusive right to produce therefrom.[9] These jurisdictions will be referred to herein as following the *qualified ownership* theory.[10]

> "Under this theory the landowner does not have title to the specific oil and gas beneath his land in severalty, nor, apparently, does he have title as tenant in common to an undivided share of the oil and gas in the common reservoir equivalent to the amount of oil and gas beneath his land. He does have, however, a co-equal right with the other landowners to the opportunity to secure his proportionate part of the oil and gas in the common reservoir by wells drilled upon his land, and a qualified title interest in the oil and gas as one of the 'collective owners.' "[11]

Under this view, since a landowner does not have *title* to the minerals under his land, of course he cannot convey a *title* to his grantee nor retain a title in himself by reservation or exception. The minerals, then, cannot be "owned" separate and apart from the surface, since such jurisdictions recognize only one fee simple estate in the land. A grant of the minerals in these jurisdictions merely gives the grantee the exclusive right to explore for and reduce the minerals to his possession, together with the surface easements necessary for mineral exploration, development and production; and the grantee gets title to the minerals only after they have been actually produced and thereby converted into personal property.[12]

Other jurisdictions, however, have adhered to the strict common law concepts of ownership of land, reiterating the maxim that a landowner owns not only the surface of the soil but everything under and above it,

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[9]Ohio Oil Co. v. Indiana, 177 U. S. 190, 20 Sup. Ct. 576, 44 L. ed. 729 (1900); Marrs v. City of Oxford, 24 F.(2d) 541 (D. Kan. 1928); Callahan v. Martin, 3 Cal.(2d) 110, 43 P.(2d) 788, 101 A.L.R. 871 (1935); Triger v. Carter Oil Co., 372 Ill. 182, 23 N.E.(2d) 55 (1939); Rupel v. Ohio Oil Co., 176 Ind. 4, 95 N.E. 225 (1911); Federal Land Bank of New Orleans v. Mulhern, 180 La. 627, 157 So. 370, 95 A.L.R. 948 (1934); Rich v. Doneghey, 71 Okla. 204, 177 Pac. 86, 3 A.L.R. 352 (1918); Barker v. Campbell-Ratcliff Land Co., 64 Okla. 249, 167 Pac. 468, L.R.A. 1918A 487 (1917).

[10]The terms *exclusive right* and *non-ownership* have also been used to designate those jurisdictions which do not consider the landowner as having title to the oil and gas in place. The term *exclusive right* is perhaps the most accurate. Although some courts and writers speak of *non-ownership*, it is submitted that the use of this term is misleading due to its implication that a landowner has no form of property rights in the oil and gas. It has been said that all courts recognize that a landowner has a property right in oil and gas which is protected by the fifth and fourteenth amendments to the Federal Constitution. See Blake, *The Oil and Gas Lease* (1940) 13 So. Calif. L. Rev. 304, 306, n. 6; Walker, *The Nature of the Property Interests Created by an Oil and Gas Lease in Texas* (1928) 7 Tex. L. Rev. 1, 2, n. 3.

[11]Walker, *Property Rights in Oil and Gas and Their Effect Upon Police Regulation of Production* (1938) 16 Tex. L. Rev. 370, 373.

[12]See cases cited in note 9 *supra*. Kulp, Cases on Oil and Gas (2d ed. 1935) c. 1; 1 Summers, Oil and Gas (Perm. ed. 1938) §§ 61, 62, 63; Blake, *The Oil and Gas Lease* (1940) 13 So. Calif. L. Rev. 304, 305.

without creating any exception to this rule in regard to oil and gas.[13] Under this, the *absolute ownership* theory, a landowner is regarded as having title in severalty to the oil and gas in place beneath his land, in the same manner that he has title to the solid minerals therein. But when it is said that a landowner has title to his oil and gas in place, but yet cannot complain when an adjoining owner drains the oil and gas from beneath his land, some explanation must be made.[14] While some courts say that these two theories cannot be reconciled, and while others recognize the inconsistency without attempting to explain or justify it, the Texas courts have announced that the two theories are not inconsistent. Thus in the leading case of *Stephens County v. Mid-Kansas Oil & Gas Co.*,[15] the Texas Supreme Court stated:

> "The objection lacks substantial foundation that gas or oil in a certain tract of land cannot be owned in place, because subject to appropriation, without the consent of the owner, of the tract, through drainage from wells on adjacent lands. If the owners of adjacent lands have the right to appropriate, without liability, the gas and oil underlying their neighbor's land, then their neighbor has the correlative right to appropriate, through like methods of drainage, the gas and oil underlying the tracts adjacent to his own. . . . Ultimate injury from the net results of drainage, where proper diligence is used, is altogether too conjectural to form the basis for the denial of a right of property in that which is not only plainly as much realty as any other part of the earth's contents, but realty of the highest value to mankind. . . ."[16]

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[13]Segars v. Goodwin, 196 Ark. 221, 117 S.W.(2d) 43 (1938); Burden v. Gypsy Oil Co., 141 Kan. 147, 40 P.(2d) 463 (1935); Hammonds v. Central Ky. Nat. Gas Co., 255 Ky. 685, 75 S.W.(2d) 204 (1934); Rathburn v. State, 285 Mich. 521, 280 N.W. 35 (1938); Willard v. Federal Surety Co., 91 Mont. 465, 8 P.(2d) 633 (1932); Pure Oil Co. v. Kendall, 116 Ohio 188, 156 N.E. 119 (1927); Hamilton v. Foster, 272 Pa. 95, 116 Atl. 50 (1922); Murray v. Allred, 100 Tenn. 100, 43 S.W. 355, 39 L.R.A. 249 (1897); Stephens County v. Mid-Kansas Oil & Gas Co., 113 Tex. 160, 254 S.W. 290, 29 A.L.R. 566 (1923); Texas Co. v. Dougherty, 107 Tex. 226, 176 S.W. 717, L.R.A. 1917F 989 (1915); Campbell v. Lynch, 81 W. Va. 374, 94 S.E. 739, L.R.A. 1918B 1070 (1917); State *ex rel.* School District No. 1 in Weston County v. Snyder, 29 Wyo. 163, 212 Pac. 758 (1923).

[14]"The true and absolute test of the ownership of a thing, on all sound legal principles, must be whether the party claiming such ownership has such right or title to the thing that no one can lawfully take it from him without his consent. If this rule is made the test, then unquestionably a landowner has no ownership of the oil and gas underlying his land." Greer, *Ownership of Oil and Gas in Place* (1923) 1 TEX. L. REV. 162, 169, reprinted in (1923) 29 W. VA. L. Q. 172. See also Simonton, *Has a Landowner Any Property in Oil and Gas in Place?* (1921) 27 W. VA. L. Q. 281; Walker, *Fee Simple Ownership of Oil and Gas in Texas* (1928) 6 TEX. L. REV. 125.

[15]113 Tex. 160, 254 S.W. 290, 292, 29 A.L.R. 566, 571 (1923).

[16]The court seems to have overlooked the fact that it could have recognized that a landowner has a "right of property" in oil and gas without holding that he has a fee simple title thereto. The courts following the qualified ownership theory recognize that a landowner has a *property right* in the oil and gas in place; they merely state that this property right is not a corporeal estate.

The Texas court's explanation has been referred to as an application of the common law doctrine of "self-help," which is followed by some jurisdictions in

Since under the absolute ownership theory a landowner has title to the oil and gas in place, a conveyance of all of his interests in the minerals will create in the grantee an absolute fee simple estate in the minerals. In like manner, an exception of the minerals from a grant of the surface estate will retain in the grantor a fee simple estate therein. The result in either case is that the land is carved into two separate and distinct corporeal fee simple estates, usually referred to as the surface estate[17] and the mineral estate.

The Mississippi Supreme Court has repeatedly approved the common law principle that "land" in legal contemplation extends from the sky to the depths of the earth, and that it includes not only the ground or soil, but everything that is attached to the soil, such as trees and buildings.[18] In accordance with this theory, it is well settled in this state that a conveyance of standing timber is a conveyance of an interest in realty, and as such must conform to the requirements of the Statute of Frauds, the homestead and recording laws, etc.[19] It has also been settled that a landowner may convey an absolute fee simple title to the standing timber on his land, and that such an estate is separate and distinct from the ownership of the surface.[20] In accord with the theory of the timber cases, the

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denying a landowner a remedy for trespass from branches overhanging his property lines. Walker, *Property Rights in Oil and Gas and Their Effect Upon Police Regulation of Production* (1938) 16 TEX. L. REV. 370, 374. Mr. Walker states that "There is no reason for giving an injured party a cause of action for the violation of some legal right resulting from a reasonable use of adjacent land if the aggrieved party's remedy of self-help is completely adequate for his proper protection." Michalson v. Nutting, 275 Mass. 232, 175 N.E. 490, 76 A.L.R. 1109 (1931) is cited as an example of the application of the "self-help" theory to overhanging branches. The inconsistency of ownership in place and nonliability for drainage has also been explained by analogy to the law of accretion. Peterson v. Grayce Oil Co., 37 S.W.(2d) 367 (Tex. Civ. App. 1931), *aff'd*, 98 S.W.(2d) 781 (Tex. 1936); 1 THORNTON, LAW OF OIL AND GAS (4th ed. 1925) 95.

[17]While the owner of the non-mineral interest is generally spoken of as the "surface owner" it is apparent, of course, that his estate is not limited to the mere surface of the land. His title extends to everything above and below the surface that is not classified as "minerals" within the meaning of the instrument creating the severance.

"After severance, the separate owners are not tenants in common. See Virginia Coal & Iron Co. v. Kelly, 93 Va. 332, 24 S.E. 1020 (1896). Nor is there any privity between them, so that either can buy the estate of the other at a tax sale. Hutchinson v. Kline, 199 Pa. 564, 49 Atl. 312 (1901)." KULP, CASES ON OIL AND GAS (2d ed. 1935) 21, n. 6.

[18]Gulf Refining Co. v. Terry, 163 Miss. 869, 886, 142 So. 457, 459 (1932); Dantzler Lmbr. Co. v. State, 97 Miss. 355, 380, 53 So. 1, 2 (1910); Butterfield Lmbr. Co. v. Guy, 92 Miss. 361, 374, 46 So. 78, 79 (1908); Fox, Tax Collector v. Pearl River Lmbr. Co., 80 Miss. 1, 6, 31 So. 583 (1902); McKenzie v. Shows, 70 Miss. 388, 389, 12 So. 336 (1893); Harrell v. Miller, 35 Miss. 700, 702 (1858).

[19]Forest Product & Mfg. Co. v. Buckley, 107 Miss. 897, 66 So. 279 (1914); Butterfield Lmbr. Co. v. Guy, 92 Miss. 361, 45 So. 78 (1908); Fox, Tax Collector v. Pearl River Lmbr. Co., 80 Miss. 1, 31 So. 583 (1902); Walton v. Lowrey, 74 Miss. 484 (1896); McKenzie v. Shows, 70 Miss. 388 (1892); Harrell v. Miller 35 Miss. 700 (1858).

[20]Forest Product & Mfg. Co. v. Buckley, 107 Miss. 897, 66 So. 279 (1914); Butterfield Lmbr. Co. v. Guy, 92 Miss. 361, 45 So. 78 (1908); Fox, Tax Collector v. Pearl River Lmbr. Co., 80 Miss. 1, 31 So. 583 (1902).

court, in the case of *Moss v. Jourdan*,[21] recognized that it is possible in this state for one person to own the minerals in place under the land separate and apart from the ownership of the surface of the land.[22]

The subsequent case of *Stern v. Great Southern Land Co.*[23] involved a petition for a partition of undivided mineral interests. The court, relying on *Moss v. Jourdan* and the timber cases, granted the partition, stating that "The deposits of clay, oil, and minerals under the surface of land, of themselves, constitute land, and are susceptible of separate ownership from the ownership of the surface of the land."[24]

The case of *Stokely v. State* ex rel. *Knox, Att'y Gen.*,[25] decided very shortly after the *Stern* case, involved the nature of the property interests created by an oil and gas lease. The court held that the instrument vested *title* to the oil in the lessee. Implicate in this decision is the assumption that the lessor owned the oil absolutely, for otherwise he certainly could not have conveyed a title thereto.

These cases might be relied upon as authority for the classification of Mississippi as a jurisdiction which recognizes the absolute ownership of oil and gas in place. It should be noted, however, that in none of these cases has the court been directly confronted with any question of drainage of oil or gas by wells on adjoining lands. And, since the denial of a recovery for drainage has been the principal reason why a number of jurisdictions have refused to recognize the absolute ownership of oil and gas in place, the Mississippi court could take a different attitude when properly confronted with the inconsistency of absolute ownership and nonliability for drainage.[26]

Under both the qualified and absolute ownership theories, if a grant of the oil and gas separate from the surface does not expressly include

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[21]129 Miss. 598, 92 So. 689 (1922). *See* Hancock County v. Imperial Naval Stores Co., 93 Miss. 822, 47 So. 177 (1908).

[22]Although the instrument under consideration in this case specified "all minerals," there was no question of the ownership of oil or gas involved, since the only point in issue was the right to remove the gravel from the land.

[23]148 Miss. 649, 114 So. 739 (1927).

[24]*Id.* at 657, 114 So. at 740.

[25]149 Miss. 435, 115 So. 563 (1928). This case will be discussed in detail in a consideration of the nature of the property interests created by the execution of an oil and gas lease, *infra* page 437.

[26]It is not very likely that the Supreme Court will take a different attitude, however. Judge McGowen wrote a dissenting opinion in the case of Gulf Refining Co. v. Terry, 163 Miss. 869, 895, 142 So. 457, 462 (1932), in which he regarded the principles announced above as settled rules of property in this state. Judges Cook and Anderson joined in this dissent. Then too, the opinion of the three judges who affirmed this case did not in any way conflict with any of the principles announced in the text above. *Cf.* Liverpool & Londan & Globe Ins. Co. v. Delaney, 200 So. 440 (Miss. 1941).

Judge Ethridge, however, in a dissenting opinion in the case of Stokely v. State *ex rel.* Knox, Att'y Gen., 149 Miss. 435, 447, 115 So. 563, 566 (1928), urged the adoption of the qualified ownership theory, although there was no question of drainage involved. This opinion relied upon numerous decisions by the United States Supreme Court which, in deference to the rule of capture, had refused to recognize absolute ownership of oil and gas in place.

the easements absolutely necessary for mineral exploration, development and production, such easements will be implied.[27] Furthermore, since such easements are strictly easements of necessity they will also be implied where the landowner reserves or excepts the minerals from a grant of the surface estate, regardless of the rule that a deed is generally construed very strictly against the grantor.[28] As a practical matter, however, it should be remembered that the owner of the mineral interest is usually much better protected when the instrument itself contains express provisions in regard to his rights to use the surface of the land, because the rights embraced in implied easements of necessity are much more restricted than those generally expressed in a mineral grant or exception.[29]

The case of *Moss v. Jourdan*,[30] however, might be classed as an exception to the general rule as to the implication of surface easements necessary for the enjoyment of the separate mineral estate. In this case there had been a grant of the surface with an exception of the minerals, but the deed made no mention of the reservation of any easements necessary for mineral exploration, development and production. The owner of the mineral estate filed a bill in equity asking for a decree enjoining the owner of the surface from interfering with his entry upon the land for the purpose of removing the minerals. It appeared that the only minerals known to be on the land were valuable deposits of gravel, and in order to remove the gravel it would have been necessary to destroy the

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[27]Richfield Oil Co. of Cal. v. Hercules Gasoline Co., 112 Cal. App. 431, 297 Pac. 73 (1931); Buck Creek R.R. v. Haws, 253 Ky. 203, 69 S.W.(2d) 333 (1934); Palmer Corp. of La. v. Moore, 171 La. 774, 132 So. 229 (1931); Henderson v. Chesley, 273 S.W. 299 (Tex. Civ. App. 1925); Squires v. Lafferty, 95 W. Va. 307, 121 S.E. 90 (1924). Oklahoma follows this rule in the case of a grant of the surface with an exception of the minerals; Ramey v. Stephney, 70 Okla. 87, 173 Pac. 72 (1918); Barker v. Campbell-Ratcliff Land Co., 64 Okla. 249, 167 Pac. 468, L.R.A. 1918A 487 (1917); but not in the case of a grant of the minerals, Newbern v. Gould, 162 Okla. 82, 19 P.(2d) 157 (1933); Morgan v. McGee, 117 Okla. 212, 245 Pac. 888 (1926). See also Bank of America Nat. Trust & Savings Ass'n v. Fisher, 61 F.(2d) 53 (C.C.A. 9th, 1932). These decisions by the Oklahoma court are not logical, to say the least.

[28]Dabney v. Child, 95 Miss. 585, 48 So. 897 (1909). The dissenting opinion in Gulf Refining Co. v. Terry, 163 Miss. 869, 895, 142 So. 457, 462 (1932), very strongly affirms this view and urges an extension of it. The majority opinion agreed with the general rule, but refused to extend it. For authorities in support of the general rule, see note 27 *supra*.

[29]For example, his rights would not be nearly as broad as those conferred by the following provisions of one mineral deed form: "together with all and singular the rights and appurtenances thereto in any wise belonging, with the right of ingress and egress and possession at all times for the purpose of mining, drilling and operating for said minerals and the maintenance of facilities and means necessary or convenient for producing, treating and transporting such minerals, and for housing and boarding employees. . . . " Another form deed gives the grantee all of the rights necessary for the purpose of "investigating, exploring, prospecting, drilling and mining for and producing oil, gas and all other minerals, laying pipe lines, building tanks, power stations, telephone lines and other structures thereon to produce, save, take care of, treat, transport and own said products, and housing its employees. . . . " See MORSE, MISSISSIPPI FORM BOOK (1940) 502, 504.

[30]129 Miss. 598, 92 So. 689 (1922).

surface of the land. As previously stated,[31] the court recognized the separate ownership of the minerals, but they refused to grant the injunction.

> "Where one person owns the surface of land and another the mineral therein, the owner of the mineral may remove it from the land, but in so doing he must allow sufficient of the subjacent land to remain to support the surface in its natural state.[32]
>
> ". . . where one person owns the surface of land and another the mineral therein, and the mineral cannot be removed without destroying the surface, the owner of the mineral, in the absence of an agreement to the contrary, is without the right to remove it."[33]

If the complainant in this case had desired to drill for and produce oil or gas, however, the court very probably would have granted the injunction, even though the exception of the minerals from the grant of the surface did not expressly reserve any surface easements. This seems to follow from the court's opinion, because the production of oil or gas does not *destroy* the surface of the land, even though it might temporarily prohibit any other use of all or a part of the surface, and even though it might completely destroy the present marketability of the land.[34] In addition, it is highly improbable that the production of oil or gas would not "allow sufficient of the subjacent land to remain to support the surface in its natural state."

Nature of the Lessee's Interest[35]

If a landowner is not regarded as owning absolutely the oil and gas under his land, any grant, exception, or lease that he might make cannot have the effect of creating a separate corporeal estate in such minerals. Under such a theory, there can be only one corporeal estate; and, there-

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[31] *Supra* page 432.

[32] 129 Miss. 598, 613, 92 So. 689, 690 (1922).

[33] *Id.* at 615, 92 So. at 691.

[34] In this connection it should be remembered that the only surface rights the complainant here would have are those easements implied by law for the necessary enjoyment of the mineral estate and that these easements would be limited to such as are reasonably necessary for the recovery of the oil and gas.

This case, however, should serve as a *caveat* to all attorneys to protect the interests of their clients purchasing or retaining separate mineral rights by expressly providing for all surface easements necessary to advantageous exploration, development and production of the oil, gas, and other minerals covered by the instrument.

See 4 SUMMERS, OIL AND GAS (Perm. ed. 1938) § 652 for a discussion of the rights of lessor and lessee to the use of the surface of the land.

[35] For general discussions of the nature of the lessee's property interests, see: MILLS AND WILLINGHAM, LAW OF OIL AND GAS (1926) §§ 48-50; 1 SUMMERS, OIL AND GAS (Perm. ed. 1938) c. 7; Blake, *The Oil and Gas Lease* (1940) 13 So. CALIF. L. REV. 304; Poole, *The Nature of the Lessee's Interest Under an Oil and Gas Lease in Kansas* (1937) 5 KAN. BAR J. 306; Simonton, *The Nature of the Interest of the Grantee Under an Oil and Gas Lease* (1918) 25 W. VA. L. Q. 295; Veasey, *The Law of Oil and Gas* (1919) 18 MICH. L. REV. 445, 749; Walker, *The Nature of the Property Interests Created by an Oil and Gas Lease in Texas* (1928) 7 TEX. L. REV. 1, (1929) 7 TEX. L. REV. 539, (1930) 8 TEX. L. REV. 483, (1932) 10 TEX. L. REV. 291, (1933) 11 TEX. L. REV. 399.

fore, an oil and gas lease can operate merely to create an encumbrance on this estate. Under the ordinary commercial oil and gas lease, the interest of the lessee is regarded by the majority of jurisdictions as an incorporeal hereditament in the nature of a *profit à prendre*.[36] This common law property interest provides a very appropriate category for the classification of an oil and gas lessee's interest, because a *profit à prendre* is the right to acquire, by severance or removal from another's land, something previously constituting a part of the realty, together with the right to do such things on the land as are reasonably necessary for the exercise of such right.[37] The creation of rights similar to those embraced in a *profit à prendre* seems to be in accordance with the intention of the parties to a mineral lease, since the purpose of such a lease is to give the lessee the exclusive right to come on the land, explore for, and produce oil, gas, or other minerals that may be found thereon. A *profit à prendre* may be appurtenant to other land, or it may be owned in gross, the latter being the usual situation in a mineral lease.[38] It may be created for an estate in perpetuity analogous to an estate in fee simple, or for any lesser period.[39] A landowner may grant this right to another, or he may reserve it himself in a conveyance of title to the land. Under this theory an oil and gas lessee gets merely the right to explore for, develop, and produce any min-

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[36]Commissioner of Internal Revenue v. McKinney, 87 F.(2d) 811 (C.C.A. 10th, 1937); Alexander v. Continental Petroleum Co., 63 F.(2d) 927 (C.C.A. 10th, 1933); Callahan v. Martin, 3 Cal.(2d) 110, 43 P.(2d) 788, 101 A.L.R. 871 (1935); Campbell v. Smith, 180 Ind. 159, 101 N.E. 89 (1913); Heller v. Dailey, 28 Ind. App. 555, 63 N.E. 490 (1902); Brinkman v. Empire Gas & Fuel Co., 120 Kan. 602, 245 Pac. 107 (1926); Willard v. Federal Surety Co., 91 Mont. 465, 8 P.(2d) 633 (1932); Homestake Exploration Corp. v. Schoregge, 81 Mont. 604, 264 Pac. 388 (1928); Rich v. Doneghey, 71 Okla. 204, 177 Pac. 86, 2 A.L.R. 352 (1918); Boatman v. Andre, 44 Wyo. 352, 12 P.(2d) 370 (1932). In Pennsylvania the nature of the lessee's interest seems to depend largely on the form of the granting clause of the lease. For example, the lessee's interest has been held to be an incorporeal hereditament, Hicks v. American Nat. Gas Co., 207 Pa. 575, 57 Atl. 55 (1904), a corporeal hereditament in the nature of a lease of the land, Barnsdall v. Bradford Gas Co., 225 Pa. 338, 74 Atl. 207 (1909), and a lease of the land with title to the oil and gas, Hamilton v. Foster, 272 Pa. 95, 116 Atl. 50 (1922).

[37]Tiedman, Real Property (3rd ed. 1906) § 424; 2 Tiffany, Real Property (2d ed. 1920) § 381; Roberts, *Inconsistencies Under the "Ownership in Place" Theory of Oil and Gas* (1940) 29 Ky. L. J. 3.

[38]2 Tiffany(Real Property § 382. Although a profit in gross cannot ordinarily be assigned so as to give each assignee the right to work it separately, this rule does not apply where the profit is exclusive and inclusive, as is a profit created by an oil and gas lease. Chandler v. Hart, 161 Cal. 405, 119 Pac. 516 (1911); New Haven v. Hotchkiss, 77 Conn. 168, 58 Atl. 753 (1904); Baker v. Kenney, 145 Iowa 638, 124 N.W. 901 (1910); Funk v. Haldeman, 53 Pa. 229 (1856); Clark, Covenants and Interests Running With Land (1929) 53, n. 4. The objection that the division of a profit in gross may result in surcharging the servient tenement does not apply to an oil and gas lease, since the servient owner's income is dependent upon the amount of production secured under the lease. The lessor, therefore, will benefit by a surcharge due to increased production. He is protected against wasteful operations by the express and implied covenants in the lease.

[39]11 Halsbury, The Laws of England (1910) 656; 2 Tiffany, Real Property § 381. For example, a *profit à prendre* created by the ordinary oil and gas lease exists for a period equivalent to a determinable fee.

erals discovered,[40] and acquires title only as personal property to minerals actually produced.[41]

If a landowner is regarded as owning the oil and gas in place, however, a lease may have the effect of creating a *profit à prendre,* or it may operate as a present conveyance of title to the oil and gas in place. The exact nature of a lessee's interest, in such a jurisdiction, will depend upon the intention of the parties as manifested by the provisions of the lease.

If the lease grants the "exclusive privilege to come upon the land and drill for oil and gas" it would seem to indicate that a *profit à prendre* is intended. If the instrument "leases and lets the land for the purpose of mining and producing oil and gas" it would indicate that the parties intended to create a "mineral lease."[42] And if the lessor "grants, bargains, sells and conveys all of the oil and gas," the provision would indicate that the instrument should operate as a conveyance of title to the oil and gas in place.

Texas is the leading jurisdiction following the absolute ownership theory of oil and gas, and for a number of years the courts of that state classified a lessee's interest in accordance with the particular phraseology of the granting clause of the lease.[43] In 1912, however, in the leading case of *Stephens County v. Mid-Kansas Oil & Gas Co.*,[44] the Supreme Court of that state announced that the usual variations found in the granting clauses of oil and gas leases would not affect the nature of the lessee's interest, stating that the parties to the different instruments all contemplated the creation of the same property interest. The court held in that case that the ordinary lease operates as a present conveyance of a corporeal estate in the oil and gas in place; and that since the lessee's interest might endure forever, and at the same time is automatically terminated upon the happening of certain events specified in the lease, the estate created is a *determinable fee.* It is not to be necessarily inferred from this case, however, that it is impossible in that jurisdiction to create by lease an interest in the oil and gas other than a corporeal estate; it only means that the ordinary commercial lease creates such an interest, and that the usual variations in phraseology in different leases are not sufficient to indicate an intention to create a different kind of interest.

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[40]2 TIFFANY, REAL PROPERTY § 385.

[41]Most leases are worded so that the lessee never gets title to the amount of oil paid as the lessor's royalty, however.

[42]Although a "mineral lease" seems to be about the same as a *profit à prendre,* some courts have not so regarded it. See, *e.g.,* Hamilton v. Foster, 272 Pa. 95, 116 Atl. 50 (1922); Barnsdall v. Bradford Gas Co., 225 Pa. 338, 74 Atl. 207 (1909). The terminology used by the court is important, however, because a lease is a corporeal interest while a profit is incorporeal.

[43]Texas Co. v. Daugherty, 107 Tex. 226, 176 S.W. 717 (1915); Witherspoon v. Staley, 156 S.W. 557 (Tex. Civ. App. 1913); Staley & Barnsdall v. Derden, 121 S.W. 1136 (Tex. Civ. App. 1909); Hodges v. Brice, 74 S.W. 590 (Tex. Civ. App. 1903); Southern Oil Co. v. Colquitt, 69 S.W. 169 (Tex. Civ. App. 1902); National Oil & Pipe Line Co. v. Teel, 95 Tex. 586, 68 S.W. 979 (1902).

[44]113 Tex. 160, 254 S.W. 290 (1923).

Thus it is seen that the fact that a particular jurisdiction follows the absolute ownership theory does not control the determination of the interest created by an oil and gas lease. And, since it appears that Mississippi will follow this theory, it would therefore be possible in this state for an oil and gas lease to operate as a grant of either a *profit à prendre* or a corporeal estate in the oil and gas.[45]

The importance of the *Stephens County* case in Mississippi law is established by the case of *Stokely v. State* ex rel. *Knox, Att'y Gen.*,[46] in which the Mississippi court adopted the Texas court's theory as to the property interests created by an oil and gas lease. The language of the opinion in the *Stokely* case followed very closely the language of the *Stephens County* case, and the latter decision was the only authority cited by the court in support of their views.

The *Stokely* case involved the power of the Board of Trustees of the state insane hospital to execute what appears to have been an ordinary oil and gas lease. It was shown that a previous statute had given the hospital the power "to receive, hold, and dispose of, all real and personal property"[47] belonging to it, but that the statute then existing provided merely that it was to "receive and hold and use"[48] its property, and that the trustees were to "have charge of the interests of the asylum, and . . . manage and direct its affairs."[49] The court construed the existing statute

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[45]That there is another possibility is indicated by the Mississippi cases involving "turpentine leases." The instruments involved in these cases were "leases" for a definite term of years of the standing pine timber for the purpose of extracting turpentine. It was held in Hancock County v. Imperial Naval Stores Co., 93 Miss. 822, 47 So. 177 (1908) that the lessee's interest under such an instrument is not taxable as real property; and in Jones v. Adams, 104 Miss. 387, 61 So. 420 (1913) that it is taxable as personal property. These cases are not a definite indication that the interest of the lessee is not an interest in real property because it is generally recognized that an interest may be regarded as real property for other purposes though not taxable as such under the statute. See, *e.g.*, Willis' Ex'r v. Commonwealth, 97 Va. 667, 34 S.E. 460 (1899) (ground rents); Note (1929) 59 A.L.R. 701 (leasehold interests). But in Newton v. Long, 107 Miss. 349, 65 So. 460 (1914), it was held on the authority of these tax cases that a turpentine lease is personal property and not required to be in writing under the statute of frauds.

On the other hand, in Gex v. Dill, 86 Miss. 10, 38 So. 183 (1905), there is some indication that a turpentine lease is an interest in realty. The court refused to cancel such a lease as a cloud on title on the ground that it was valid. There is thus a possible indication that an invalid lease would have constituted a cloud on title, and that it is thus an interest in realty, since an interest in personalty of cannot ordinarily constitute a cloud on title.

For cases involving turpentine leases which did not decide the nature of the property interests created, see Harrison Naval Stores Co. v. Adams, 104 Miss. 381, 61 So. 417 (1913); Union Naval Stores Co. v. Adams, 104 Miss. 299, 61 So. 419 (1913); Jones v. Adams, 61 So. 419 (Miss. 1913); Orrell v. Bay Mfg. Co., 83 Miss. 800, 36 So. 561 (1903).

These cases may conceivably have some possible influence on the interpretation oil and gas leases, but their significance in this regard is considered extremely doubtful. Both the subject matter and the language of these instruments are materially different from the ordinary oil and gas lease, and it is particularly noteworthy that all of the leases were for a definite term of years.

[46]149 Miss. 435, 115 So. 563 (1928).

[47]Miss. Rev. Code (1871 § 2073.

[48]Miss. Code Ann. (1892) § 2807 [Miss. Code Ann. (1930) § 4549].

[49]Miss. Code Ann. (1892) § 2812 [Miss. Code Ann. (1930) § 4545].

to mean that the board did not have the power to dispose of the hospital property and held that they were therefore without statutory authorization to execute the oil and gas lease in question.[50] In determining the effect of the lease under consideration, the court stated:

> "Under this instrument the title to seven-eighths of the oil in the land is vested in the grantee. . . . Under the provisions of the instrument the rights conferred thereby continue so long as oil or gas, or either of them, is produced on said land, provided drilling was commenced by a fixed date. Under this provision, the termination of the grant is wholly uncertain, and the rights granted may endure forever. . . . For an able and elaborate discussion of an analogous question, and a collation of the authorities which support the view herein expressed, see the case of *Stephens County v. Mid-Kansas Oil & Gas Co.* . . ."[51]

Justice Ethridge wrote a dissenting opinion, relying on the provision of the statute giving the Board of Trustees the power to "receive and hold and use" the hospital property, and contended that a liberal construction of the word *use* would provide sufficient statutory authorization for the execution of such a lease. He cited authority to the effect that the grant of the use of property is not a grant of the property itself, the user having merely the right to hold, occupy, and receive the benefit thereof; and contended that the majority should have held this lease to be a mere use of the land, since it was the manifest intention of the legislature to restrict only the alienation of the *corpus* of the soil itself. The dissent also quoted from some of the numerous cases holding that oil and gas in place are not subject to absolute ownership; whence is to be concluded that if the state did not own the oil and gas under the hospital lands, the lease in question could not have operated as a conveyance of title thereto.

Although the dissenting opinion did not expressly contend that the lease should have been construed as creating a *profit à prendre,* it would seem that this would have been a convenient means of upholding the trustee's authority to execute this lease, since the lease then would not take effect as an alienation of the corpus of the land itself.

Since the *Stokely* case represents such a direct and express approval of the theory of the Texas courts, as established in the *Stephens County* case, and since Mississippi appears to be the only other jurisdiction that has approved this view, a more detailed consideration of the exact holding of these two cases may be helpful. Although the language of the opinion in the *Stokely* case is very similar to that of the *Stephens County* case, the Mississippi court was not as definite as the Texas court, in that the *Stokely* case did not attempt expressly to classify the lessee's estate in the termin-

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[50]It is interesting to note that the legislature has recently vested title to the Insane Hospital property in the Mineral Lease Commission, which has the express power to execute oil and gas leases. Miss. Laws 1932, c. 114, Miss. Code Ann. (Supp. 1938) § 1777.

[51]Stokely v. State *ex rel.* Knox, Att'y Gen., 149 Miss. 435, 446, 115 So. 563, 566 (1928).

ology of real property law. The Texas court expressly held that the lessee's estate was a determinable fee in the oil and gas. The Mississippi court stated (1) that "title to seven-eighths of the oil in the land is vested in the grantee," (2) that "termination of the grant is wholly uncertain," and (3) that "the rights granted may endure forever." Is the effect of this holding different in any respect from that of the *Stephens County* case?

A fee simple estate is the only kind of a fee interest in land that is recognized in Mississippi, since a statute[52] prohibits the creation of estates in fee tail. It is clearly possible in this state, however, to have a fee estate that is subject to special limitation[53] or to conditions subsequent[54] or to both.

Every estate known to the common law is subject to certain *general* limitations which determine the quantum or duration of the estate granted. At common law, the words *and his heirs* were words of general limitation in a grant of a fee estate, the limitational event being the death of the owner without heirs and without having disposed of the property. It is possible, however, that the estate may be subject to certain additional limitations expressed in the grant, usually classified as *special limitations.* A special limitation is an event the happening of which will *ipso facto* terminate the grantee's estate before the happening of the general limitation.[55] Any estate or interest in land may be subject to one or more special limitations expressed in the instrument of conveyance creating the estate. A fee simple estate subject to a special limitation, however, is generally referred to as a *determinable fee.*[56] Such an estate is usually created by a grant or devise *so long as* or *while* an existing state of things shall endure, or until a certain event takes place.[57]

Any estate or interest in land may also be created subject to various conditions subsequent. An estate subject to a condition subsequent is one which may be terminated by the creator of the estate, or his successor in interest, on the occurrence of some event, the happening of which may or may not be controllable by the holder of the estate.[58] A condition subsequent is usually introduced by such words as *but if, on condition that, provided that,* or *so that.*[59]

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[52]Miss. Code Ann. (1930) § 2117.

[53]Hamilton v. City of Jackson, 157 Miss. 284, 127 So. 302 (1930). See also Kirby v. Calhoun, 16 Miss. 462 (1847).

[54]Kent v. Stevenson, 127 Miss. 529, 90 So. 241 (1922); Wright v. Hardy, 76 Miss. 524, 24 So. 697 (1898); Memphis & Charleston R.R. v. Neighbors, 51 Miss. 412 (1875); Gadberry v. Sheppard, 27 Miss. 203 (1854).

[55]1 Restatement, Property (1936) § 23; 1 Simes, Law of Future Interests (1936) § 177; 1 Tiffany, Real Property § 90.

[56]1 Restatement, Property (1936) § 16.

[57]1 Restatement, Property (1936) § 23; 1 Tiffany, Real Property § 91.

[58]Kent v. Stevenson, 127 Miss. 529, 90 So. 241 (1922); Memphis & Charleston R.R. v. Neighbors, 51 Miss. 412 (1875); 1 Restatement, Property (1936) § 24; 1 Simes, Law of Future Interests (1936) § 159; 1 Tiffany, Real Property §§ 74, 76.

[59]1 Tiffany, Real Property § 78.

Every fee estate must be of potentially infinite duration. Therefore in the grant of a determinable fee or a fee subject to a condition subsequent, the event named in the special limitation or condition subsequent must be of such a nature that it may possibly never happen.[60]

It is very important to distinguish between an estate subject to a special limitation and an estate subject to a condition subsequent. A special limitation is a limit on the duration of the estate granted. When the limitational event occurs, the estate *ipso facto* terminates, regardless of any act or intention of the parties. The effect of the occurrence of the event named in a condition subsequent is very different, however, in that the estate does not automatically terminate. The happening of the event merely gives the grantor, or his heirs, the power to terminate the estate by taking affirmative action, such as a reentry on the land, notice to the holder of the estate, or an action in court.[61] Since a determinable fee estate terminates by virtue of an express limit on the quantum of the estate, there is no *forfeiture* of the estate, and the equitable principles of forfeiture have no application. In a fee subject to condition subsequent, however, the enforcement of the grantor's right of entry for condition broken results in a divestment of the estate, and a court of equity will intervene where possible to prevent the enforcement of such a forfeiture.[62]

The grantor of a determinable fee retains a possibility of reverter; the grantor of an estate subject to a condition subsequent retains a right

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[60]This possibility, however, is of a legal rather than a physical character. For example, the classical illustration of a determinable fee is a grant to *A* so long as St. Paul's Church shall stand, or to *A* so long as a certain tree shall stand. The fact that it is a physical impossibility for the church or tree to stand forever will not prevent the estate from being a fee. 1 SIMES, LAW OF FUTURE INTERESTS (1936) § 180; 1 TIFFANY, REAL PROPERTY § 93.

[61]Kent v. Stevenson, 127 Miss. 529, 90 So. 241 (1922); Memphis & Charleston R.R. v. Neighbors, 51 Miss. 412 (1875); 1 RESTATEMENT, PROPERTY (1936) § 24, comment *b*, §§ 57, 58; 1 SIMES, LAW OF FUTURE INTERESTS (1936) § 160; 1 TIFFANY, REAL PROPERTY § 75.

[62]Yazoo & M. V. R.R. v. Lakeview Traction Co., 100 Miss. 281, 56 So. 393 (1911); Buck v. City of Macon, 85 Miss. 580, 37 So. 460 (1904); Miller v. Tunica County Supervisors, 67 Miss. 651, 7 So. 429 (1890); Memphis & Charleston R.R. v. Neighbors, 51 Miss. 412 (1875); Gadberry v. Sheppard, 27 Miss. 203 (1854); 1 RESTATEMENT, PROPERTY (1936) § 56; 1 TIFFANY, REAL PROPERTY §§ 85, 88; Walker, *The Nature of the Property Interests Created by an Oil and Gas Lease in Texas* (1930) 8 TEX. L. REV. 483, 529. This distinction has not been recognized by some courts. See, *e.g.*, Gloyd v. Midwest Refining Co., 62 F.(2d) 483 (C.C.A. 10th, 1933); Liddle v. Cook, 209 Fed. 182 (C.C.A. 8th, 1913); Brewster v. Lanyon Zinc Co., 140 Fed. 801 (C.C.A. 8th, 1905); Kays v. Little, 103 Kan. 461, 175 Pac. 149, 1 A.L.R. 675 (1918); Brazell v. Soucek, 130 Okla, 204, 266 Pac. 442 (1928); Oldfield v. Gypsy Oil & Gas Co., 123 Okla. 293, 253 Pac. 298 (1927).

In drafting an instrument to create a condition subsequent it is wise to provide expressly that the grantor or his heirs shall have a right to reenter as of their former estate upon the happening of the event. Although such a provision should not be required, some courts have held that the absence of such a clause is an indication of the intention of the parties to create a mere *covenant*, for the breach of which damages alone can be recovered. See *e.g.*, *In re* Matter of Copps Chapel Methodist Episcopal Church, 120 Ohio St. 309, 166 N.E. 218 (1929).

of entry for condition broken.[63] Neither of these interests is an estate in land; each is a mere expectancy, the possibility of becoming an estate upon the happening of certain events.

Before a determinable fee or a fee subject to a condition subsequent has terminated, the owner of the estate has all of the rights of an owner in fee simple absolute.[64]

With these characteristics of a determinable fee in mind, let us now consider the language of the Mississippi court in the *Stokely* case. In the first place, the court said that "title to seven-eighths of the oil in the land is vested in the grantee." This language clearly indicates that the grantee has a proprietary interest in the oil, and the requisites of a fee estate are certainly satisfied by the statement that "the rights granted may endure forever." And, since the "termination of the grant is wholly uncertain," it would seem that this fee estate is subject to certain special limitations, *i.e.,* that it is a determinable fee, because it is of potentially infinite duration and yet may possibly terminate at any time upon the occurrence of one of the limitational events. The principal special limitations on this estate, of course, are the provisions of the habendum clause of the lease designating that the estate is granted for a specific purpose[65] (mineral exploration and production) and is to exist for a term of years and as long thereafter as oil or gas is produced.[66]

Additional support for the contention that the effect of the holding in the *Stokely* case is that the lease conveyed a determinable fee in the oil and gas lies in the fact that the language in the opinion followed so closely the language of the Texas court in the *Stephens County* case, and the fact that the only authority cited was the "elaborate discussion of an analogous question" found in the Texas case. The *Stokely* case also followed the *Ste-*

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[63]1 SIMES, LAW OF FUTURE INTERESTS (1936) §§ 159, 177. The Restatement uses the term *power of termination* instead of *right of entry for condition broken.* 1 RESTATEMENT, PROPERTY (1936) § 24,, comment *b.*

Although neither a possibility of reverter nor a right of entry for condition broken was alienable at common law, they can be assigned in Mississippi. Hamilton v. Jackson, 157 Miss. 284, 127 So. 302 (1930); Wright v. Hardy, 76 Miss. 524, 24 So. 697 (1898).

[64]Memphis & Charleston R.R. v. Neighbors, 51 Miss. 412 (1875).

[65]The courts seem to regard a conveyance for mineral purposes and an ordinary grant for a specified purpose differently, since the mere recitation of the purpose of a grant will not usually operate as a limitation on the estate. Thornton v. City of Natchez, 88 Miss. 1, 41 So. 498 (1906); Raley v. Umatilla County, 15 Ore. 172, 13 Pac. 890 (1887); Magnolia Petroleum Co. v. Jackson, 82 S.W.(2d) 1011 (Tex. Civ. App. 1935); Hughes v. Gladewater County Line Independent School District, 76 S.W.(2d) 471 (Tex. Comm. App. 1934); Note (1913) 44 L.R.A. (N.S.) 1222; *cf.* Soria v. Harrison County, 96 Miss. 109, 50 So. 443; Buck v. City of Macon, 85 Miss. 580, 37 So. 460 (1904).

[66]An additional limitation is found in the ordinary oil and gas lease where the delay rental clause is in the "unless" form, because the estate can also terminate automatically under this clause by the failure of the lessee to commence drilling within the stated period or to pay the specified delay rental. McDaniel v. Hager-Stevenson Oil Co., 75 Mont. 356, 243 Pac. 582 (1926); Waggoner Estate v. Sigler Oil Co., 118 Tex. 509, 19 S.W.(2d) 27 (1929); Humble Oil & Refining Co. v. Davis, 296 S.W. 298 (Tex. Comm. App. 1927); Note (1930) 67 A.L.R. 223.

phens County case in saying that the particular phraseology of the granting clause of the lease does not vary the nature of the estate conveyed.

> "From a practical standpoint, the rights of the grantee under an instrument which conveyed the oil and gas under the land and granted the exclusive right to conduct operations to produce and dispose of the same, or under an instrument which leased, demised, and let the land for the same purpose, would be no other, different, or greater than the rights of the grantee in the instrument here involved, and we are of the opinion that this instrument is, in legal effect, a lease of the land and a conveyance of an interest therein."[67]

This language makes it appear that the usual variations in the wording of oil and gas leases will not be an important factor in determining the legal effect of the instrument. Although this holding is commendable for furnishing a degree of stability to the legal effect of mineral leases, and although it probably reflects the usual intention of the parties, it should not be extended, however, beyond the *usual* variations in the phraseology of such leases. It should not be authority to the effect that it is impossible to vary the nature of the interest granted, because a different result should certainly be possible if the intention to create some other interest is very clearly and unmistakably expressed.[68]

It is true, however, that the court further stated that "this instrument is, in legal effect, a lease of the land and a conveyance of an interest therein." If the court really meant that this instrument operated as a true lease of the land, it is very difficult to reconcile this statement with the other language of the opinion. The statements previously discussed seem to indicate that the court regarded the instrument as a conveyance of title to the oil and gas subject to certain special limitations, which render what would otherwise have been an absolute fee simple a determinable fee. If this view is correct, the instrument would in no manner operate as a true "lease" of the land.[69] Possibly the court only meant by this statement that the lease conveyed an interest in the surface of the land itself in addition to the conveyance of title to the minerals. It is true that the lease conveys very valuable rights to the use of the surface of the land, but the land is not *leased* for this purpose. These surface rights are in the nature of easements appurtenant to the mineral estate.

The conclusions drawn from the *Stokely* case are: (1) that under the ordinary oil and gas lease the interest conveyed to the lessee is a de-

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[67]Stokely v. State *ex rel.* Knox, Att'y Gen., 149 Miss. 435, 447, 115 So. 563, 566 (1928).

[68]For example, it has been held than an instrument which leases all of the pine timber on the land for the purpose of extracting turpentine does not pass an interest in land taxable as realty. Hancock County v. Imperial Naval Stores Co., 93 Miss. 822, 47 So. 177 (1908). See also Orrell v. Bay Mfg. Co., 83 Miss. 842, 36 So. 561, 70 L.R.A. 881 (1904).

[69]*Cf.* Barnsdall v. Bradford Gas Co., 225 Pa. 338, 74 Atl. 207, 27 L.R.A. (N.S.) 614 (1909) in which the court regarded a similar instrument as a demise of the land and a conveyance of title to the oil and gas.

terminable fee, (2) that this interest is a present, vested, corporeal[70] estate in the oil and gas[71] in place.

The effect of the lease is to divide the land into two separate and distinct possessory estates, in the same manner that an absolute deed to the minerals creates two separate estates. This severance by lease differs from a severance by absolute deed, however, in that under most leases the lessee obtains title to only seven-eighths[72] of the oil, whereas the grantee of a mineral deed obtains title to all of the oil and all of the gas. The question of whether the lessee obtains title to all or only a part of the oil and gas depends upon the provisions of the royalty clause of the particular lease under consideration. Under the ordinary lease, the granting clause gives the lessee title to all of the oil and gas,[73] but this clause is limited by the royalty clause which usually provides that the lessee is to pay the lessor one-eighth of all oil produced, to be delivered to the credit of the lessor in pipe lines or in storage.[74] Since the lessee then has no right to one-eighth of the oil as such, it is held that the lessor retains title to this portion.[75] If, however, the lease provides that the lessee is to pay, or at his option can pay, the lessor the market value of one-eighth of the oil, then the lessee obtains title to all of the oil in place, since the lessee then has a right to retain all of the oil as such.[76] Practically all of the leases provide that the royalty on gas, casinghead gas, and all other minerals, shall be payable in money, thereby vesting title to all of such minerals in the lessee. If the lessor has the option to demand payment of the royalty in either kind or money, he then retains title to that portion of the minerals.[77]

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[70]The use of the word *title* shows that the court regarded the lessee's estate as corporeal.

[71]Although the lease in the *Stokely* case itself did not convey title to the *gas*, this was not due to any difference in the physical nature of oil and gas, or to any difference in the legal relations thereto. This holding was based upon the peculiar provisions of this particular lease, *i.e.*, that all gas produced from the land should belong to the hospital, but that the lessee should have the right to purchase it after production at a specified price.

[72]For purposes of discussion, it is assumed that the lessor has a royalty of one-eighth on both oil and gas.

[73]The lease in the *Stokely* case was different, however, in that the lessee did not get title to the gas. See note 71 *supra*.

[74]It is interesting to note that under this type of royalty clause the lessee is under no duty to pay the lessor anything for the oil produced. The lessee fulfills his duty when he delivers the royalty oil in the pipe line or in storage. The lessor usually executes a division order authorizing the pipe line company to take his royalty oil at field prices, thereby relying on the credit of the pipe line company for payment for his oil.

[75]Sheffield v. Hogg, 124 Tex. 290, 77 S.W.(2d) 1021 (1934); Hager v. Stakes, 116 Tex. 453, 294 S.W. 835 (1927); Corsicana Petroleum Co. v. Owens, 110 Tex. 568, 222 S.W. 154 (1920); Walker, *The Nature of the Property Interests Created by an Oil and Gas Lease in Texas* (1931) 8 Tex. L. Rev. 291; Note (1934) 13 Tex. L. Rev. 501.

[76]*Ibid.*

[77]Regardless of whether the lessor's royalty is payable in kind or money, it is still regarded as real property for most purposes. Sheffield v. Hogg, 124 Tex. 290, 77 S.W.(2d) 1021 (1934); Blake, *Oil Royalties: A Suggested Criterion*, this issue, *supra* page 307; Blake, *The Oil and Gas Lease* (1940) 13 So. Calif. L. Rev. 393, 410; Walker, *The Nature of the Property Interests Created by an Oil and Gas Lease in Texas* (1931) 8 Tex. L. Rev. 291; Note (1934) 13 Tex. L. Rev. 501.

The grantee's estate under a lease also differs from his estate under a mineral deed in that his fee estate is determinable under the former and absolute under the latter. In addition, an oil and gas lease also contains certain conditions subsequent and numerous express and implied covenants not usually present in a mineral deed.[78]

Adverse Possession

The concept of separate possessory estates in the surface and minerals becomes important in a consideration of the effect of adverse possession of the land. If there has been no separation of the surface and mineral interest, the adverse possession of the surface of the land for the statutory period of time will, of course, vest title to the surface and minerals in the adverse possessor.[79] If there has been a mineral deed or lease, however, the adverse possession of the surface of the land for the statutory period of time does not vest title to the minerals in the adverse possessor.[80] Although this rule is universally recognized, most of the courts have not attempted to analyze the reasons behind it, but have contented themselves with the conclusion that adverse possession of the surface is not adverse possession of the minerals. In some of the cases it is said that the reason for the rule is that mere possession of the surface is not *adverse* to the separate mineral interest. This reasoning is correct if the jurisdiction does not recognize the creation of a separate possessory estate in the minerals, because the claimant's possession of the surface will be actual possession of the single corporeal estate. If the jurisdiction holds that a separate possessory estate in the oil and gas is created, however, it would seem that the correct reason for the adverse possession rule is that possession of the surface of the land is not *possession* of the corporeal mineral estate.[81] This distinction is important, because it does not matter what

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[78]For the distinction between a mineral deed and a lease, see 1 SUMMERS, OIL AND GAS (Perm. ed. 1938) § 132.

[79]This arises from the maxim, *Cujus est solum, ejus est usque ad coelum et ad inferos* (He who owns the land owns also to the sky and to the depths). Broughton v. Humble Oil & Refining Co., 105 S.W.(2d) 480 (Tex. Civ. App. 1927); Kiser v. McLean, 67 W. Va. 294, 67 S.E. 725 (1910).

[80]Morse v. Schackleford, 9 F.(2d) 907 (C.C.A. 6th, 1926); Louisville & N. R.R. v. Massey, 136 Ala. 156, 33 So. (1903); Claybrooke v. Barnes. 180 Ark. 678, 22 S.W.(2d) 390 (1929); Rendro v. Hanon, 297 Ill. 353, 130 N.E. 740 (1921); Gray-Mellon Oil Co. v. Fairchild, 219 Ky. 143, 292 S.W. 743 (1927); Gordon v. Park, 202 Mo. 236, 100 S.W. 621 (1907); Murray v. Allred, 100 Tenn. 100, 43 S.W. 355, 39 L.R.A. 249 (1897); Yates v. State, 3 S.W.(2d) 114 (Tex. Civ. App. 1928); Elliott v. Nelson, 113 Tex. 62, 251 S.W. 501 (1923); Wallace v. Elm Grove Coal Co., 58 W. Va. 449, 52 S.E. 485 (1905); Note (1921) 13 A.L.R. 375.

[81]It is also frequently stated that adverse possession of the surface will not vest title to the separate mineral interest because the owner of the minerals has no *remedy* against the trespasser on the surface. This begs the question, however, regardless of the nature of the mineral owner's interest. If the mineral owner has a separate *possessory* estate, he will have a remedy in ejectment if the adverse possessor of the surface takes *possession* of the minerals. If the mineral owner does not have a separate possessory estate, he will still have a remedy if the adverse possessor asserts a claim of ownership of the minerals inconsistent with the mineral owner's exclusive right of production.

acts [82] the adverse possessor commits on the surface of the land indicating his claim of ownership of the minerals if he has never been in possession of the mineral estate. He must take possession of the mineral estate before the statute will begin to run against the mineral owner, and apparently the only way he can acquire such possession is by drilling wells into the producing stratum.[83]

If a separate possessory mineral estate has been created, the fact that the adverse possessor of the surface claims the minerals under color of title will not be sufficient to give him constructive possession of the minerals. Color of title will not give an adverse possessor constructive possession of a part of the land not actually occupied by him unless all of the land so claimed belonged to the same owner.[84] A landowner is not affected with notice of a constructive possession of his land by the fact that it is included in a conveyance with other land not belonging to him, unless some part of the land owned by him is occupied by the claimant.

Where the severance of the estates is by means of a lease in which the surface owner retains title to one-eighth of the oil in place, the adverse possession of the surface will also vest title to one-eighth of the oil because there has been no severance of the estates as to this portion.[85]

If the owner of the surface estate is the lessor in an oil and gas lease, and if a stranger obtains title to the surface by adverse possession, the question then arises as to whether the adverse possessor or the lessor is entitled to the delay rentals and royalties payable under the lease and to the mineral rights after the termination of the lease. As previously discussed, the lessor, in addition to his rights to delay rentals and royalties, has a possibility of reverter in the minerals. This possibility of reverter, however, is entirely separate and apart from the ownership of the surface and is appurtenant or incident to the mineral and not the surface estate. Therefore, upon the termination of the lease, the lessor and not the new surface owner will obtain the title to all of the oil and gas not removed under the lease. In like manner, the royalties and delay rentals are incident to the ownership of the mineral and not the surface estate,[86] and the

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[82]In Mississippi, adverse possession must be hostile, actual, open, notorious, exclusive, and continuous for a ten year period. MISS. CODE ANN. (1930) § 2287; Breland v. O'Neal, 88 Miss. 449, 40 So. 865 (1906); McCaughn v. Young, 85 Miss. 277, 37 So. 839 (1905).

[83]Bodcaw Lmbr. Co. v. Goode, 160 Ark. 48, 254 S.W. 345, 29 A.L.R. 578 (1923); Hoskins v. Northern Lee Oil & Gas Co., 194 Ky. 628, 240 S.W. 377 (1922); Henderson v. Chesley, 229 S.W. 573 (Tex. Civ. App. 1921); Lyles v. Dodge, 228 S.W. 316 (Tex. Civ. App. 1921); Kiser v. McLean, 67 W. Va. 294, 67 S.E. 725 (1910); Note (1921) 13 A.L.R. 372.

[84]Leavenworth v. Reeves, 106 Miss. 722, 64 So. 660 (1914); Mitchell v. Boyd, 84 Miss. 72, 36 So. 148 (1904); Jones v. Gadis, 67 Miss. 769, 7 So. 489 (1890); Note (1889) 2 L.R.A. 277; 2 TIFFANY, REAL PROPERTY 1990. § 512.

[85]Walker, *The Nature of the Property Interests Created by an Oil and Gas Lease in Texas* (1929) 7 TEX. L. REV. 539, 578.

[86]It is to be noted, however, that if the surface is conveyed without expressly reserving the benefits under an existing oil and gas lease, the grantee will be entitled to receive the delay rentals, royalties, and the possibility of reverter under the lease. The grantee does not acquire these rights because they pass as incident to the surface estate, however. He acquires the benefits of the lease because they

adverse possessor by acquiring title to the surface estate would not be entitled to receive any of the income arising from the lease.[87] The rule is different, however, where the lessor *retains title* to one-eighth of the oil in place.[88] Since there has been no severance of the estates as to this portion of the oil, the adverse possessor of the surface acquires title thereto, and, therefore, would be entitled to receive the oil royalties under the lease. For the same reason, upon the termination of the lease, the adverse possessor remains the owner of the amount of oil fixed as royalty, although he acquired no rights in the possibility of reverter in the balance.

Partition

The theory of the existence of separate possessory estates in the surface and minerals becomes important in determining the rights of cotenants to secure an involuntary partition of their interests. Most courts will not grant a partition in kind of separately owned mineral interests nor of the land itself if it is known to contain oil and gas.[89] Such jurisdictions state that it would be impossible to make an equitable partition of the mineral interests, and the only remedy available is a partition by sale.

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are included within the *description* of the land conveyed, *i.e.*, unless otherwise expressed, a conveyance includes all of the grantor's interests in the described land, and a description of land includes everything from the depths of the earth to the skies. It is held that the mere recitation that the grant is "subject to" the existing lease is not a sufficient indication of the intention of the grantor to reserve his rights as lessor. Empire Gas & Fuel Co. v. Higgins Oil & Fuel Co., 279 Fed. 977 (C.C.A. 5th, 1922); Osborn v. Arkansas Territorial Oil & Gas Co., 103 Ark. 175, 146 S.W. 122 (1912); Clark v. Richfield Oil Co. of Calif., 127 Cal. App. 495, 16 P.(2d) 162 (1932); Chandler v. Pittsburgh Plate Glass Co., 20 Ind. App. 165, 50 N.E. 400 (1898); Keystone Gas Co. v. Allen, 227 Ky. 801, 14 S.W.(2d) 155 (1929); Northwestern Ohio Natural Gas Co. v. Ullery, 68 Ohio St. 259, 67 N.E. 494 (1902); White v. McVey, 168 Okla. 19, 31 P.(2d) 850, 94 A.L.R. 656 (1934); Hinds v. McCord, 45 S.W.(2d) 442 (Tex. Civ. App. 1931); Bibb v. Nolan, 6 S.W.(2d) 156 (Tex. Civ. App. 1928); Stephenson v. Glass, 276 S.W. 1110 (Tex. Civ. App. 1925), *writ of error denied*, 115 Tex. 192, 279 S.W. 260 (1926); Japhet v. McRae, 276 S.W. 669 (Tex. Comm. App. 1925); Robinson v. Jacobs, 113 Tex. 231, 254 S.W. 309 (1923); Musgrave v. Musgrave, 86 W. Va. 119, 103 S.E. 302, 16 A.L.R. 564 (1920); Walker, *The Nature of the Property Interests Created by an Oil and Gas Lease in Texas* (1928) 7 TEX. L. REV. 1. *Contra:* Wettengel v. Gormley, 184 Pa. 354, 39 Atl. 57 (1898).

[87]Walker, *The Nature of the Property Interests Created by an Oil and Gas Lease in Texas* (1929) 7 TEX. L. REV. 539, 578. If the lease is held to create an incorporeal hereditament, however, there has been no severance of the estates; and the adverse possessor who obtains title to the surface should be held to be entitled to the royalties and delay rentals under the lease, and to the unencumbered mineral fee upon the termination of the lease.

[88]See text page 443 *supra.*

[89]Dangerfield v. Caldwell, 151 Fed. 554, 81 C.C.A. 400 (C.C.A. 4th, 1907); Union Gas & Oil Co. v. Wiedman Oil Co., 211 Ky. 361, 277 S.W. 323 (1925); Gulf Refining Co. v. Hayne, 138 La. 555, 70 So. 509, L.R.A. 1916D 1147; Preston v. White, 57 W. Va. 278, 50 S.E. 236 (1905); Hall v. Vernon, 47 W. Va. 295, 34 S.E. 764, 49 L.R.A. 464 (1899). See authorities collected in Notes (1934) 91 A.L.R. 210, (1926) 40 A.L.R. 1408, (1925) 39 A.L.R. 741. 3 SUMMERS, OIL AND GAS (Perm. ed. 1938) § 536. The mere fact that the land may contain oil and gas will not prevent a partition in kind, however, even though such a partition necessarily results in a partition of any minerals therein. Morley v. White, 93 W. Va. 682, 118 S.E. 135 (1923).

By statute in Mississippi "Partition of land held by joint-tenants, tenants in common, or coparceners, having an estate in possession or a right of possession . . . may be made by decree of the chancery court."[90] Under this statute cotenants of a mineral estate are clearly entitled to involuntary partition. The important question that arises, however, is whether it is possible in this state to secure a judicial partition in kind of the mineral estate, or whether the tenants must resort to a partition by sale under order of the court. Section 2924 of the Mississippi Code provides that "If, upon hearing, the court be of opinion that a sale of the lands, or any part thereof, will better promote the interest of all parties than a partition in kind, or if the court be satisfied that an equal division cannot be made, it shall order a sale of the lands, or such part thereof as may be deemed proper and a division of the proceeds among the co-tenants according to their respective interests." It has been well settled that a sale of land and a division of the proceeds thereof among the cotenants will not be ordered under this statute unless the land is not susceptible of partition in kind, and that the burden is on the tenant seeking such sale to show that it is not susceptible of partition in kind.[91]

In the case of *Stern v. Great Southern Land Co.*,[92] however, the Mississippi Supreme Court refused to apply this rule to the partition of a separate mineral estate. The petitioner in this case was the owner of all of the surface of the land and of an undivided half interest in the minerals therein. The defendant was the owner of the other undivided half interest in the minerals. The bill alleged that the deposits of minerals under the land were not susceptible of partition in kind, and that a sale of the land and division of the proceeds thereof was therefore necessary. On the trial, however, no evidence was introduced to show that there could not be an equal division in kind of the minerals. The defendant objected to a sale of the mineral estate on the ground that, as a condition precedent to the authority of the court to order a sale of an interest in land, the statute requires a showing that partition in kind would not be equitable. The court recognized this to be the general rule, but stated that it had no application here.

> "But there are some things that do not require proof; they are self evident, and we think *the very character and nature of the interests in the land sought here to be sold make it self-evident that they are not susceptible of partition in kind* among the co-tenants owning it. . . . As to where such deposits [of minerals] are, whether under the entire surface of the land, or only a part of it, would, of course, be a mere matter of opinion, and could not be ascertained, positively, without an expensive mining operation which might cover months, and possibly, years. To partition the deposits of clay, oil, and minerals here involved, if feasible,

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[90]Miss. Code Ann. (1930) § 2920.

[91]Hague v. Armstrong, 159 Miss. 875, 132 So. 446 (1931); Hilburn v. Hilburn, 134 Miss. 235, 98 So. 593 (1924); Shorter v. Lesser, 98 Miss. 706, 54 So. 155 (1911); Smith v. Stansel, 93 Miss. 69, 46 So. 538 (1908).

[92]148 Miss. 649, 114 So. 739 (1927).

> it seems could only be done through an expensive and protracted mining scheme inaugurated and carried out by the chancery court."[93]

While it is recognized that a strict interpretation of this opinion would probably reflect the views of the majority of other jurisdictions,[94] it is suggested that the holding in this case should not be arbitrarily applied in all partition cases involving undivided interests in oil and gas. In fact, if this case is carried to its logical conclusion, it would mean that it would be impossible to obtain a partition in kind of any land known to contain *any* minerals.

It is not altogether correct to say that the "very character and nature" of the mineral interests "make it self-evident that they are not susceptible of partition in kind." There are no peculiar characteristics of mineral interests that make them inherently incapable of partition in kind. Every partition of land in which there has been no severance necessarily involves a partition of the minerals therein, and it is clear that a voluntary partition of such interests will be enforced by the courts regardless of whether the land is known to contain minerals. No reason is perceived why a voluntary partition of severed mineral interests should not also be enforced.[95] Furthermore, every involuntary partition in kind where there has been no severance, automatically involves a partition of all minerals contained therein, and it is clear that in the normal case the court will favor such a decree. This leaves us with the question involved in the following situations: (1) where the land is not known[96] to contain minerals and where there has been no severance; (2) where the land is not known to contain minerals but there has been a severance; (3) where the land is known to contain minerals and there has been no severance; (4) where the land is known to contain minerals and there has been a severance. In the first situation the court would readily grant a partition in kind. In like manner, such a decree should be granted in the second case, since the mineral rights of the cotenants would be distributed in exactly the same manner as in the first situation. The circumstances of the third case, however, might make it inequitable to enter a decree of partition in kind of the mineral interests. But the fact that the land is known to contain minerals should not compel the cotenants to accept a partition by sale of their *surface* estate. Therefore, in this situation it would seem that the only fair partition might be a partition in kind of the surface and a partition by sale

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[93]148 Miss. 649, 658, 114 So. 739, 740 (1927). Italics added.

[94]See authorities cited in note 89 *supra.*

[95]In enforcing a voluntary partition, the court need not be concerned with the fairness of the allotment. If the requirements of the statute are met, the agreement will be binding and conclusive on the parties. MISS. CODE ANN. (1930) § 2919. See Byers v. Byers, 183 Pa. 509, 38 Atl. 1027 (1898); Stevenson v. Yoho, 63 W. Va. 144, 59 S.E. 954 (1907); Note (1916) L.R.A. 1916D 1154.

[96]It is impossible, of course, to "know" that any particular tract of land contains oil or gas unless there has been actual production thereon. It would always be a question of fact for the trial court as to whether there were sufficient *indications* of the presence of oil, gas, or other minerals in the land to classify the tract as "known" mineral land.

of the mineral.[97] It may well be that in the fourth case the only equitable decree would be for partition by sale of the mineral interests and division of the proceeds thereof. The decree in *each* situation, however, should depend upon the particular circumstances of the case, and should not be controlled by any arbitrary rule, such as announced in the *Stern* case. These suggestions are merely applications of the general rules of partition, *i.e.*, that equity favors a partition in kind and will always grant such a decree unless it would be inequitable to do so under the particular circumstances of the case.[98]

The court in the *Stern* case objected to a partition in kind because of the fact that there had been no development of the minerals, and, therefore, it would have been impossible to determine what portions of the land in fact contained any minerals. In the case of *Henderson v. Chesley*,[99] however, involving an identical ownership situation, the Texas Court of Civil Appeals reached the opposite result. The court in that case stated that since there had been no mineral exploration it should be assumed for the purpose of partition that each acre of land contained an equal amount of minerals.[100] In affirming this case,[101] the Texas Supreme Court pointed out that it is not necessary that the holding of each mineral owner be represented by only one division or allotment; if a division in various allotments ("checkerboarding") would be more equitable, this procedure might be followed. Although the statute under which this partition was granted was very similar to the present Mississippi statute, the Texas Legislature later enacted a statute[102] expressly providing for a partition in kind of mineral interests. Under this statute, the court has granted a

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[97]The statute provides that the court "may decree the sale of a part of the land and the partition in kind of the residue." MISS. CODE ANN. (1930) § 2924.

[98]"The common law gave the joint owners of land a right to have a partition in kind; and the right of selling the land, and dividing the proceeds, given by the statute, is an innovation upon the common law, and as it takes away from the owner the right to keep his freehold in kind, it must be strictly pursued, and it must appear from the record that an equal division cannot be made, or that a sale of the land will better promote the interests of all parties than a partition in kind." Cox v. Kyle, 75 Miss. 667, 669, 23 So. 518, 519 (1898). Hilburn v. Hilburn, 134 Miss. 235, 98 So. 593 (1924); Shorter v. Lesser, 98 Miss. 706, 54 So. 155 (1911); Smith v. Stansel, 93 Miss. 69, 46 So. 538 (1908); Tindall v. Tindall, 3 So. 581 (Miss. 1888); 4 POMEROY, EQUITY JURISPRUDENCE (4th ed. 1919) § 1390.

"The burden was on the [party requesting a partition by sale] to show that the lands were not susceptible of partition in kind." Hague v. Armstrong, 159 Miss. 875, 881, 132 So. 446, 448 (1931).

[99]273 S.W. 299 (Tex. Civ. App. 1925).

[100]Evidence of geological or geophysical surveys of the land would, of course, be admissible to overcome this presumption. If such evidence tends to show that each acre does not have an equal amount of minerals, then the allotment should be made with this in mind, giving each co-owner his proportionate part of the favorable and unfavorable structures.

[101]Henderson v. Chesley, 116 Tex. 355, 292 S.W. 156 (1927).

[102]TEX. STAT. (Vernon, 1936) Art. 6082.

partition in kind of mineral rights where there were producing wells on the property.[103]

Abandonment

The question of whether an oil and gas lease creates a possessory estate or only an incorporeal hereditament is very important in considering the manner in which the interest may be lost by abandonment. If the interest is an incorporeal hereditament, such as an easement or a *profit à prendre,* it may be lost by a voluntary relinquishment or non-user, although an intention to abandon is usually required.[104] It is well settled by the common law, however, that title to a vested corporeal estate cannot be lost by abandonment, even though an intention to abandon is proved.[105] Therefore, if an oil and gas lease creates a fee estate, as the holding in the *Stokely* case indicates, such estate cannot be lost by mere non-user.

There is a very important distinction between the divestment of an estate by abandonment and the termination of an estate by the happening of a special limitational event. Since an oil and gas lease conveys the minerals for a specific purpose, *i.e.,* mineral exploration and production, and since this purpose creates a special limitation on the lessee's estate, the limitational event will occur when this purpose is no longer pursued.[106] The

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[103]Goodloe & Meredith v. Harris, 95 S.W.(2d) 1141 (Tex. Comm. App. 1936); Humble Oil & Refining Co. v. Lasseter, 95 S.W.(2d) 730 (Tex. Civ. App. 1936). Partition in kind of oil and gas interests has also been allowed under this statute in the following cases: Johnson v. Bussey, 95 S.W.(2d) 990 (Tex. Civ. App. 1936); Moore v. Blackwell, 85 S.W.(2d) 980 (Tex. Civ. App. 1935); McKee v. McKee, 12 S.W.(2d) 849 (Tex. Civ. App. 1928); Rolls v. Woods, 291 S.W. 532 (Tex. Comm. App. 1927); Caldwell v. Farrier, 248 S.W. 425 (Tex. Civ. App. 1923); Gee v. Lyles, 233 S.W. 640 (Tex. Civ. App. 1921). Partition in kind of undivided mineral rights has also been allowed in the following cases from other jurisdictions: Manley v. Boone, 87 C.C.A. 197, 159 Fed. 633 (C.C.A. Alaska, 1908); Royston v. Miller, 76 Fed. 50 (C.C.D. Nev. 1896); Mitchell v. Cline, 84 Cal. 409, 24 Pac. 164 (1890); Ryan v. Egan, 26 Utah 241, 72 Pac. 933 (1903).

[104]Matthews Slate Co. v. Advance Industrial Supply Co., 172 N. Y. Supp. 830 (1918), commented on in (1919) 32 HARV. L. REV. 735; CLARK, COVENANTS AND INTERESTS RUNNING WITH LAND (1929) 57; 2 TIFFANY, REAL PROPERTY § 277. As to loss of lessee's interest by abandonment, see Venture Oil Co. v. Fretts, 152 Pa. 451, 25 Atl. 152 (1893); 1 SUMMERS, OIL AND GAS (Perm. ed. 1938) § 171. In Louisiana the lessee's right may be lost by non-user for the prescriptive period. Palmer Corp. of La. v. Moore, 171 La. 774, 132 So. 229 (1930) and the authorities therein cited; DAGGETT, MINERAL RIGHTS IN LOUISIANA (1939) § 11.

[105]Tenn. Oil Co. v. Brown, 131 Fed. 696, 65 C.C.A. 524 (C.C.A. 6th, 1904); Rarver v. Deppen, 132 Ga. 798, 65 S.E. 177, 24 L.R.A. (N.S.) 1161 (1910); Barrett v. Kansas & Texas Coal Co., 70 Kan. 649, 79 Pac. 150 (1905); Glynn v. Maxfield, 75 N.H. 482, 76 Atl. 196 (1910); Kreamer v. Voneida, 213 Pa. 74, 62 Atl. 518 (1905), *aff'd,* 24 Pa. Super 347 (1904); 1 C.J. p. 10, § 14.

[106]It is also important to distinguish between abandonment and the breach of the implied covenant to develop the premises reasonably. For breach of the implied covenant, the lessor's remedy is ordinarily an action at law for damages. Texas Pacific Coal & Oil Co. v. Barker, 117 Tex. 418, 6 S.W.(2d) 1031, 60 A.L.R. 936 (1928); Texas Co. v. Curry, 229 S.W. 643 (Tex. Civ. App. 1921); Grubb v. McAfee, 109 Tex. 212 S.W. 464 (1919); Fisher v. Crescent Oil Co., 178 S.W. 905 (Tex. Civ. App. 1915). Also see MERRILL, COVENANTS IMPLIED IN OIL AND GAS LEASES (2d ed. 1940) c. 7.

estate is then terminated, not by virtue of any common law principles of abandonment, but by the happening of one of the events which limit the duration of the estate.[107] Therefore, if there has been a total non-user of the estate for a period which would be sufficient to constitute abandonment in the case of an incorporeal interest, then there would also have been an occurrence of the limitational event in the determinable fee estate.

This question becomes important in determining whether there can be a *partial* abandonment of the leased premises. For example, one producing well in a remote corner of the lease will be sufficient to fulfill the limitational requirement that the land be devoted to mineral exploration, development and production, although the lessee may not have conducted any activities of any kind on any of the other portions of the lease.[108] Although some of the Texas cases have indicated that the lessee might lose his title to the other portions of the lease by abandonment,[109] this should not be possible under common law principles. The remedy of the lessor in such a case should be an action at law for damages for the breach of the implied *covenant* to develop the premises with reasonable diligence.[110] In addition, the lessor is sometimes given a unique remedy in the form of a decree requiring the lessee to drill exploratory wells on specified portions of the land under penalty of forfeiture of his lease as to such portions by decree of the court — a remedy entirely unknown to the common law.[111]

Taxation

Taxation of the mineral interest is expressly provided by for statute in Mississippi.[112] Although this statute expressly includes any mineral interest owned separately and independently of any interests in the surface,

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[107]Texas Co. v. Davis, 113 Tex. 321, 254 S.W. 304 (1923); *cf.* Waggoner Estate v. Sigler Oil Co., 118 Tex. 509, 19 S.W.(2d) 27 (1929). Walker, *The Nature of the Property Interests Created by an Oil and Gas Lease in Texas* (1930) 8 Tex. L. Rev. 483, 493 *et seq.*

[108]Leonard v. Prater, 36 S.W.(2d) 216, 86 A.L.R. 499 (Tex. Comm. App. 1931); Rendleman v. Bartlett, 21 S.W.(2d) 58 (Tex. Civ. App. 1929); Mon-Tex Corp. v. Poteet, 118 Tex. 546, 19 S.W.(2d) 32 (1929).

[109]Waggoner Estate v. Sigler Oil Co., 118 Tex. 509, 19 S.W.(2d) 27 (1929); Cox v. Sinclair Gulf Co., 265 S.W. 196 (Tex. Civ. App. 1924); Chapman v. Ellis, 254 S.W. 615 (Tex. Civ. App. 1923); Russell v. Brooks, 254 S.W. 404 (Tex. Civ. App. 1923).

[110]See authorities cited in note 106 *supra.*

[111]This technique was first suggested by way of dictum in Grubb v. McAfee, 109 Tex. 527, 212 S.W. 464 (1919) and Waggoner Estate v. Sigler Oil Co., 118 Tex. 509, 19 S.W.(2d) 27 (1929), and has been followed in Union Sulphur Co. v. Texas Gulf Sulphur Co., 42 S.W.(2d) 182 (Tex. Civ. App. 1931); Scott v. Jackson, 37 S.W.(2d) 1068 (Tex. Civ. App. 1931); Leonard v. Prater, 36 S.W.(2d) 216, 86 A.L.R. 499 (Tex. Comm. App. 1931); Lido Oil Co. v. Waggoner Estate, 31 S.W.(2d) 154 (Tex. Civ. App. 1930); Rendlemen v. Bartlett, 21 S.W.(2d) 58 (Tex. Civ. App. 1929).

[112]"Whenever any ... mineral, gas, coal, oil ... or similar interests in real estate ... are owned separately and apart from and independently of the rights and interests owned in the surface of such real estate, or when any person reserves any right or interest, or has any leasehold in the elements above enumerated, all of such

the interest of a lessor or royalty holder who does have an interest in the surface might also be considered as taxable under this section.[113] If this is true, it would allow a landowner to have his surface estate assessed separately from any interests he might own in the minerals as lessor. This would allow a landowner to prevent a tax sale of his rights as lessor by the payment of the assessments thereon even though he did not desire to pay the taxes on his surface estate. If any separate assessment of the mineral interest is made under this statute the valuation of the surface should be correspondingly diminished so as to avoid double taxation of the minerals.[114]

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interests shall be assessed and taxed separately from such surface rights and interests in said real estate, and shall be sold for taxes in the same manner and with the same effect as other interests in real estate are sold for taxes. . . . " MISS. CODE ANN. (1930) § 3146.

[113]The statute could apply where any interest is owned separately from the surface, "or when any person reserves any right or interest . . . in the elements above enumerated."

[114]See Hancock County v. Imperial Naval Stores Co., 93 Miss. 822, 47 So. 177 (1908), where the court recognized the impropriety of double taxation of the same economic interest in land.

Capacity Necessary to Execute an Oil and Gas Lease in Mississippi[1]

The various jurisdictions which have been confronted with a determination of the property interests created by the execution of an ordinary oil and gas lease have not agreed upon the exact nature of the interest conveyed to a lessee.[2] Most of them have decided that a lessee under an ordinary oil and gas lease has an incorporeal hereditament in the nature of a *profit à prendre*.[3] Others have ruled that the ordinary oil and gas lease is a true lease of the land for mining purposes.[4] A third view is that an ordinary oil and gas lease conveys to the lessee a determinable fee simple estate in the oil and gas in place.[5] Apparently all of the jurisdictions, with one exception,[6] seem to agree that such an instrument passes a present interest in land.[7]

In the only Mississippi case which is directly in point, *Stokely v. State*,[8] it was held that an oil and gas lease passes an interest in land. In that case, the court said, "Under this instrument the title to 7/8 of the oil in the land is vested in the grantee . . . this instrument is, in legal effect, a lease of the land and a conveyance of an interest therein."[9]

Once it has been determined that the lessee obtains an interest in land, there are very few instances in which the exact nature of the interest

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[1]While this note is confined to the execution of oil and gas leases, much of what is included herein will be applicable to the execution of deeds, leases, or conveyances of any other interest in land.

The term *capacity* as used in this title refers to the individual qualifications of the lessor and to the nature of the interest in land which he must possess in order to make a valid oil and gas lease.

[2]See 1 Summers, Oil and Gas (Perm. ed. 1938) § 152; Walker, *The Nature of the Property Interests Created by an Oil and Gas Lease In Texas* (1929) 7 Tex. L. Rev. 1.

[3]Lake v. Sealy, 231 Ala. 466, 165 So. 399 (1936); Standard Oil Co. v. Oil Well Salvage Co., 170 Ark. 729, 281 S.W. 360 (1926); Callahan v. Martin, 3 Cal.(2d) 110, 43 P.(2d) 788 (1935); Heller v. Dailey, 28 Ind. App. 555, 63 N.E. 490 (1902); Burden v. Gypsy Oil Co., 141 Kan. 147, 40 P.(2d) 463 (1935); Rich v. Donaghey, 710 Okla. 204, 177 Pac. 86 (1918); Boatman v. Andre, 44 Wyo. 352, 12 P.(2d) 370 (1932).

[4]Woodland Oil Co. v. Crawford, 55 Ohio St. 161, 44 N.E. 1093 (1896); Barnsdall v. Branford Gas Co., 225 Pa. 338, 74 Atl. 207 (1909). See also Morris v. Mosser, 156 Tenn. 54, 299 S.W. 782 (1927); Petroleum Co. v. Coal, Coke & Mfg. Co., 89 Tenn. 381, 18 S.W. 65 (1890).

[5]Stephens County v. Mid-Kansas Oil & Gas Co., 113 Tex. 160, 254 S.W. 290 (1923). The case of Stokely v. State, 149 Miss. 435, 115 So. 563 (1928) follows this case very closely, quoting and citing it with approval. For a discussion of the *Stokely* case and the Mississippi view as to the nature of the lessee's interest see Note, *Property Rights in Oil and Gas in Mississippi*, *supra* page 434, this issue.

[6]Walla Walla Oil, Gas & Pipe Line Co. v. Vallentine, 103 Wash. 359, 174 Pac. 980 (1918).

[7]1 Summers, Oil and Gas (Perm. ed. 1938) § 153; Walker, *The Nature of the Property Interests Created by an Oil and Gas Lease in Texas* (1928) 7 Tex. L. Rev. 562. But see Hutchinson v. McCue, 101 F.(2d) 111, 116 (C.C.A. 4th, 1939) where the court said, "It is well settled that a lessee of an oil and gas lease in West Virginia acquires in the first instance a mere license or inchoate right to go upon the land and explore for oil and gas; but after oil and gas is found, the lessee acquires a vested estate therein."

[8]149 Miss. 435, 115 So. 563 (1928).

[9]*Id.* at 446, 115 So. at 566.

conveyed is material in ascertaining the capacity necessary to the execution of an oil and gas lease. Generally speaking, the same principles apply to, and the same formalities must be present for, the execution of a valid conveyance of any kind of interest in land. Inasmuch as there are very few Mississippi cases shedding any light on the question of the requisite capacity to execute an oil and gas lease, the precedents must be found in the cases involving other types of conveyances. It must be recognized, however, that the Supreme Court of Mississippi may not see fit to be bound by its decisions regarding conveyances in general when deciding cases involving oil and gas leases because of the inherently different physical characteristics of oil and gas.

The most important instances in which the question of capacity to execute arises are situations involving leases by: (1) Infants or their Guardians; (2) Insane Persons or their Guardians; (3) Life Tenants; (4) Tenants in Common; (5) Husband or Wife (of Homesteads); (6) Persons Acting Under Powers; (7) the State (of Public Lands).

1. *Leases by Infants or Their Guardians*

The general common law rule as to conveyances by a minor is applicable, and it is generally held that an oil and gas lease executed by an infant is voidable and may be avoided by him before reaching majority.[10] The minor may ratify the lease after becoming of age either expressly or by his conduct.[11] And the statute of limitations does not begin to run against the minor until his disability is removed.[12] There are no Mississippi cases concerning oil and gas leases executed by infants, but the principles are the same as in cases of other kinds of conveyances by infants.[13]

Mississippi statutes[14] provide for the removal of disability of minors in the chancery court of the county of their residence, or in the chancery court of a county in which a non-resident minor owns real estate or any interest in real estate.[15] Of course, any lease executed after such removal would be on the same plane as leases by adults.

In the case of ordinary contracts by infants, a distinction is drawn in Mississippi between executed and executory contracts. Executed contracts

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[10]2 SUMMERS, OIL AND GAS (Perm. ed. 1938) § 212. The Mississippi law as to infants' contracts is exhaustively treated in Notes (1936) 9 MISSISSIPPI LAW JOURNAL 217, (1937) 9 MISSISSIPPI LAW JOURNAL 484.

[11]Self v. Prairie Oil & Gas Co., 28 F.(2d) 590 (C.C.A. 8th, 1938); Teat v. Jones, 89 S.W.(2d) 987 (Tex. Comm. App. 1936); Humble Oil & Refining Co. v. Clark, 126 Tex. 262, 87 S.W.(2d) 471 (1935).

[12]This is expressly provided in MISS. CODE ANN. (1930) § 2308.

[13]For Mississippi cases on conveyances by infants see Dulion v. Folkes, 153 Miss. 91, 120 So. 437 (1929); McLeiter v. Rackley, 148 Miss. 75, 114 So. 128 (1927); Ferguson v. Bobo, 54 Miss. 121 (1876); Wallace v. Latham, 52 Miss. 291 (1876); Brantley v. Wolf, 60 Miss. 420 (1832). See also Notes (1936) 9 MISSISSIPPI LAW JOURNAL 217, (1937) 9 MISSISSIPPI LAW JOURNAL 484.

[14]MISS. CODE ANN. (1930) §§ 353-357.

[15]Such removal of disability does not empower a minor to demand a conveyance of a trustee who holds land by deed directing a conveyance to the minor when he becomes of age. Ray v. Kelly, 82 Miss. 597, 35 So. 165 (1903). The Chancery Court has the power to remove the disability of a person under fourteen years of age. McLeiter v. Rackley, 148 Miss. 75, 114 So. 128 (1927).

must be disaffirmed or they will become obligatory; executory contracts must be affirmed or they will be null.[16] It seems probable that this distinction would be adhered to by the court in dealing with oil and gas leases, and it would appear that a contract by an infant to execute an oil and gas lease must be affirmed or it will be void.

The maximum length of time allowed by statute in Mississippi for ordinary leases by a guardian of land belonging to his ward is three years, but the period of the lease may not extend beyond the time the minor becomes of age.[17]

The Mississippi statute[18] confers on guardians the special power to execute oil and gas and mineral leases "when it would be for the interest of an infant or insane person." The guardian must file a petition in the chancery court, setting forth the reasons why such lease should be made and the benefits to be derived therefrom. Leases executed under the authority of this statute may be upon such terms and for such length of time as may be for the best interests of the estate of the ward.[19] Such leases may be executed "in consideration of the payment of an annual rental and/or a royalty or a part or portion of the production thereof." All such leases are subject to the approval of the chancellor.

In Texas, by statute, an oil and gas lease executed by the guardian of a minor is not allowed to extend beyond the time that the minor will become of age, "unless at that time the lessee shall have discovered such minerals as are specified in the lease," in which case the lease remains in full force so long as such minerals or any of them are produced in paying quantities.[20] Such a statute is not a severe restriction on the power to lease the land, since it is usually possible to have a minor's disability removed if the minor is so near to majority that the lessee would not have a sufficiently long exploratory term within which to find oil before the minor becomes of age.

A similar limitation on the term of the lease in Mississippi seems advisable, especially in view of the Mississippi statute[21] providing that a lease may be executed in consideration of the payment of an annual rental or a royalty. Under the present Mississippi statute, a guardian could execute a lease with a long primary or exploratory term which would run after the ward attained majority in consideration of future royalties only,

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[16]Edmunds v Mister, 58 Miss. 765 (1881). See discussion in Notes (1936) 9 Mississippi Law Journal 217, (1937) 9 Mississippi Law Journal 484.

[17]Miss. Code Ann. (1930) § 1878.

[18]Miss. Code Ann. (1930) § 1879.

[19]Kentucky has a somewhat similar statute in respect to the terms of the lease. Ky. Stat. Ann. (Carroll, 1936) §§ 2031a-2 to 2031a-6.

There would apparently be some confusion in determining who could execute an oil and gas lease on the land of a married infant over 18 years of age. By Sec. 1892, Miss. Code Ann. (1930), the powers of the guardian over the estate of the ward cease when such an infant marries, and it has been held that the ward in such a situation is not by the statute enabled to contract generally as an adult. Chapman v. Hughes, 61 Miss. 339 (1883).

[20]Tex. Stat. (Vernon, 1936) Art. 4192.

[21]Miss. Code Ann. (1930) § 1879.

and with no provision for delay rentals. In such a situation the ward's only relief seems to lie in the implication by the court of a covenant to develop,[22] or possibly the implication of a limitation based upon the lack of development.[23] This relief may well be unsatisfactory for the reason that, while the courts have shown an increasing willingness to imply such covenants, it is by no means certain that they would do so in any particular case.[24]

2. *Leases by Insane Persons or Their Guardians*

Ordinary contracts and conveyances executed by insane persons are generally considered voidable,[25] though some jurisdictions look to the extent of mental incapacity to determine whether they are void or merely voidable.[26]

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[22]Sauder v. Mid-Continent Petroleum Corp., 292 U. S. 272, 78 L. ed. 1255, 54 Sup. Ct. 671 (1934); Cosden Oil Co. v. Scarborough, 55 F.(2d) 634 (C.C.A. 5th, 1932); Ezzell v. Oil Associates, 180 Ark. 802, 22 S.W.(2d) 1015 (1930); Becker v. Submarine Oil Co., 55 Cal. App. 698, 204 Pac. 245 (1922); Daughtee v. Ohio Oil Co., 263 Ill. 518, 105 N.E. 308 (1914); Webb v. Croft, 120 Kan. 654, 244 Pac. 1033 (1926); Central Kentucky Natural Gas Co. v. Williams, 249 Ky. 242, 60 S.W.(2d) 580 (1933); Doiron v. Calcasien Oil Co., 172 La. 553, 134 So. 742 (1931); Berthelote v. Loy Oil Co., 95 Mont. 434, 28 P.(2d) 187 (1933); Broswood Oil & Gas Co. v. Mary Oil & Gas Co., 164 Okla. 200, 23 P.(2d) 387 (1933); Highfield Co. v. Kirk, 248 Pa. 19, 93 Atl. 815 (1915); Texas Pacific Coal & Oil Co. v. Barker, 117 Tex. 418, 6 S.W.(2d) 1031, 60 A.L.R. 936 (1928); Hays v. Bowser, 110 W. Va. 323, 158 S.E. 169 (1931). For a discussion of the implied covenants in an oil and gas lease, see MERRILL, COVENANTS IMPLIED IN OIL AND GAS LEASES (2d ed. 1940) c. III; Walker, *The Nature of the Property Interests Created by an Oil and Gas Lease in Texas* (1933) 11 TEX. L. REV. 399. And see the annotation of cases in (1934) 93 A.L.R. 460.

[23]Texas Co. v. Davis, 113 Tex. 321, 254 S.W. 304 (1923); Hickernell v. Gregory, 224 S.W. 691 (Tex. Civ. App. 1920); Fisher v. Crescent Oil Co., 178 S.W. 905 (Tex. Civ. App. 1915); J. M. Guffey Petroleum Co. v. Oliver, 79 S.W. 884, 888 (Tex. Civ. App. 1904); Benavides v. Hunt, 79 Tex. 383, 15 S.W. 396 (1891); 3 SUMMERS, OIL AND GAS (Perm. ed. 1938) § 461.

[24]This situation arose from no-term leases. See Campbell v. Rock Oil Co., 151 Fed. 191 (C.C.A. 7th, 1907); Consumers Gas Trust Co. v. Crystal Window Glass Co., 163 Ind. 190, 70 N.E. 366 (1904); Mid-South Oil Co. v. Jaynes, 298 Ky. 483, 271 S.W. 553 (1925); Murdock-West Co. v. Logan, 69 Ohio St. 514, 69 N.E. 984 (1904); Rosson v. Bennett, 294 S.W. 660 (Tex. Civ. App. 1927); Johnson v. Armstrong, 81 W. Va. 399, 94 S.E. 753 (1917).

[25]Texas and Louisiana adhere to this general view in regard to oil and gas leases executed *prior* to a judicial adjudication of insanity. Reiners v. Humble Oil & Refining Co., 192 La. 415, 188 So. 47 (1939); Free v. Owen, 131 Tex. 138, 113 S.W.(2d) 1221 (1938); Neill v. Pure Oil Co., 101 S.W.(2d) 402 (Tex. Civ. App. 1937); Murphy v. Johnson, 54 S.W.(2d) 158 (Tex. Civ. App. 1932).

A majority of the courts have held that after an insane person has been adjudicated insane, his contracts and conveyances are void and not merely voidable. Hellman Commercial Trust & Savings Bank v. Alden, 206 Cal. 592, 275 Pac. 794 (1929); Burgedorf v. Hamer, 95 Neb. 113, 145 N.W. 250 (1914); MADDEN, PERSONS AND DOMESTIC RELATIONS (1931) § 235.

For application of this rule to oil and gas leases see Elston v. Jasper, 45 Tex. 409 (1876).

[26]In 32 C.J. 742, § 528 it is said: "Some authorities, in determining whether the conveyance of an insane person, whose incapacity has not been judicially adjudicated, is void or merely voidable, have seen proper to consider the character or quantum of the grantor's mental incapacity. . . . In accordance with such

In Mississippi, a party contracting with an insane person is not entitled to protection as an innocent purchaser or incumbrancer without notice of insanity, simply because he did not know of the mental incapacity at the time of the making of the contract of conveyance;[27] nor is the restoration of the *status quo ante* a condition precedent to disaffirmance.[28]

In determining whether a contract may be avoided by one *non compos mentis,* the Mississippi courts will consider the extent of the mental incapacity in relation to the particular transaction in question.[29] Oil and gas leases are of such a complicated nature that it would seem that a fairly high degree of intelligence would have to be shown in order to uphold the validity of the lease.

Since the six-year statute of limitations in Mississippi[30] does not begin to run against a person of unsound mind until after he regains sanity,[31] an insane person's right to avoid an oil and gas lease is not barred unless there have been six years of sanity after the execution of the lease. This saving, however, does not extend longer than twenty-one years.[32]

Insofar as guardians of insane persons are concerned, they are empowered by statute[33] to execute oil and gas leases when it would be for the interest of the insane ward, provided a petition for such purpose is approved by the chancellor.

3. *Leases by Life Tenant or Remainderman, or Both*

According to the settled rules of real property, a life tenant may not commit voluntary waste on the land in which he has a life estate.[34] He is entitled only to the use of the land and its income and is not allowed to take any of the corpus of the land. For the same reasons the cutting of

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test, it is held that in order to render the deed entirely void there must exist an entire want of understanding; but the deed of a person who is not entirely without understanding, but merely feeble-minded or the like, is not void but merely voidable."

[27]Woolbert v. Lee Lumber Co., 151 Miss. 56, 117 So. 354 (1928).

[28]Woolbert v. Lee Lumber Co., 151 Miss 56, 117 So. 354 (1928); Ricketts v. Joliff, 62 Miss. 440 (1884).

[29]In Ricketts v. Joliff, 62 Miss. 440, 448 (1884), the court said: "Weakness of understanding is not of itself any objection to the validity of a contract if the capacity remains to see things in their true relations and to form correct conclusions. The doubtful and uncertain point at which the disposing mind disappears and where incapacity begins can be ascertained only by an examination of all the circumstances of each particular case, to be duly weighed and considered by the court or jury and in determining the question the common sense and good judgment of the tribunal must be mainly relied on."

[30]Miss. Code Ann. (1930) § 2292.

[31]*Id.* § 2308.

[32]*Ibid.*

[33]Miss. Code Ann. (1930) § 1879. For the power of the guardian over real estate of the insane person, exclusive of power to execute oil and gas lease see Miss. Code Ann. (1930) § 1902.

[34]2 Thompson, Real Property (2d ed. 1939) 528. § 819: For Mississippi cases on waste by life-tenant see Learned v. Ogden, 80 Miss. 769, 32 So. 278 (1902); Cannon v. Barry, 59 Miss. 289 (1881). See also Kimbrough, *Law of Waste in Mississippi Territory and State* (1935) 7 Mississippi Law Journal 234.

timber or the digging of solid minerals constitutes voluntary waste, so does the removal of oil and gas.[35] Since, therefore, a life tenant does not himself have the authority to extract oil and gas, he cannot give that right to someone else.

However, a life tenant is entitled to the rents *and* royalties from wells drilled *prior* to the creation of the life estate.[36] Furthermore, if an oil and gas lease has been executed prior to the creation of the life estate, the life tenant is entitled to the rents and royalties (not merely the interest on them) accruing during the life estate under such lease.[37] He has these rights by virtue of the notion that a life tenant is entitled to the profits of the land *as determined by the use to which the land has been put.*[38]

A remainderman does not have the right to possession of the land and cannot, therefore, enter upon the land in order to drill for oil and gas without the consent of the life tenant; nor can he confer that right on another.[39]

However, a valid lease may be executed by the life tenant and the remainderman acting together.[40] Moreover, a lease executed by a life tenant alone may be ratified by acts of the remainderman, such as the acceptance of delay rentals or royalties;[41] and the remainderman may be estopped to question the right of the life tenant to exploit the property for oil and gas or confer the right of exploitation on another.[42] The lessee may deal separately with the life tenant and the remainderman. He may secure an oil and gas lease from the remainderman, subject to the life estate, and one from the life tenant conferring on him the right to use the land in such manner that he may develop it by drilling. The two leases would be the equivalent of one executed jointly by the life tenant and the remainderman.[43]

If the life tenant refuses to join in the execution of an oil and gas lease, and the oil is being drained away, the remainderman can probably

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[35]2 THOMPSON, REAL PROPERTY (2nd ed. 1939) 535, § 825; Minner v. Minner, 84 W. Va. 679, 100 S.E. 509 (1919).

[36]Fairbanks v. Warrum, 56 Ind. App. 337, 104 N.E. 983 (1914); Richmond Natural Gas Co. v. Davenport, 37 Ind. App. 25, 76 N.E. 525 (1905); Andrews v. Andrews, 31 Ind. App. 189, 67 N.E. 461 (1903); Benson v. Nyman, 136 Kan. 455, 16 P.(2d) 963 (1934); Woodburn's Estate, 138 Pa. 606, 21 Atl. 16 (1891); Minner v. Minner, 84 W. Va. 679, 100 S.E. 509 (1919); Campbell v. Lynch, 81 W. Va. 374, 94 S.E. 739 (1917); Koen v. Bartlett, 41 W. Va. 559, 23 S.E. 664, 31 L.R.A. 128 (1895).

[37]Minner v. Minner, 84 W. Va. 679, 100 S.E. 509 (1919). See also annotations in (1926) 43 A.L.R. 811 *et seq.*

[38]Cherokee Construction Co. v. Harris, 92 Ark. 260, 122 S.W. 485, (1909); Ellis v. Flanagan, 279 Ill. 93, 116 N.E. 618 (1917); Drier v. Gracey, 203 Mich. 399, 169 N.W. 835, 171 N.W. 749 (1918). For the Mississippi view see Kimbrough, *Law of Waste in Mississippi Territory and State* (1935) 7 MISSISSIPPI LAW JOURNAL 234.

[39]4 THOMPSON, REAL PROPERTY (2d ed. 1939) 736, § 2203.

[40]Union Gas & Oil Co v. Weidemann Oil Co., 211 Ky. 361, 277 S.W. 323 (1924).

[41]Burden v. Gypsy Oil Co., 141 Kan. 147, 40 P.(2d) 463 (1935).

[42]Williams v. Jones, 43 W. Va. 562, 27 S.E. 411, 38 L.R.A. 694 (1897.

[43]Orndorff v. Consumers' Fuel Co., 308 Pa. 165, 162 Atl. 431 (1932).

get relief in a court of equity by obtaining authority to execute a lease, paying interest on the rents and royalties to the life tenant.[44]

4. *Leases by Cotenants*

It is well settled that a joint lease made by all cotenants is a valid oil and gas lease on the common property.[45] Likewise, a lessee may obtain the same rights by securing a lease from each of the cotenants severally.[46]

However, the various jurisdictions are not in agreement as to the right of one cotenant to execute a completely valid oil and gas lease of his rights in the common property without the joinder of the other cotenants. The right of one cotenant to execute a lease conferring the right of drilling on a third party depends, of course, upon his right to drill himself.

As in the situation involving a life tenant, the laws of waste are important in determining the rights of a cotenant. By the early common law a cotenant could not be guilty of committing waste.[47] However, most of the states have either enacted statutes conferring a right of action against a cotenant committing waste or have permitted such an action to be maintained, and have granted injunctions preventing waste.[48] There are no statutes on this subject in Mississippi, but it has been held[49] that such a remedy will be granted. Each cotenant is entitled to possession or user of the common property as long as he does not exclude the others and as long as his use of the property does not result in its destruction or consumption. As the extraction of oil and gas consumes part of the corpus of the land, it would seem to constitute waste just as in the case of a life tenancy, unless prior to the creation of the cotenancy the land has been devoted to this purpose so as to constitute the oil and gas normal profits of the land.[50]

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[44]Simonton, *Right of Remainderman to Compel Life Tenant to Permit Development of Oil and Gas* (1920) 26 W. Va. L. Q. 213; Walker, *Fee Simple Ownership of Oil and Gas in Texas* (1928) 6 Tex. L. Rev. 125, 143.

A somewhat similar remedy was granted by the English courts when timber on the land was rotting and the life tenant refused to cut it. 1 Tiffany, Real Property (2d ed. 1920) 955.

[45]Vaughan v. McCool, 186 Miss. 549, 191 So. 286 (1940); Crory v. Campbell, 24 Cal. 634 (1864); Hayden v. Patterson, 51 Pa. 261 (1865); Tiedman, Real Property (3d ed. 1906) 250, § 189.

[46]Miles v. Fink, 119 Miss. 147, 80 So. 532 (1919); Lee Chuck v. Quan Won Tong, 91 Cal. 593, 28 Pac. 45 (1891); Barnum v. Landon, 25 Conn. 137 (1856).

[47]Walker, *Fee Simple Ownership of Oil and Gas* (1928) 6 Tex. L. Rev. 125, 145. In 1285, however, a right of action for waste was given by Stat. Westminister II.

[48]27 R.C.L. 1040, § 31; Tiffany, Real Property (2d ed. 1920) 990; Note (1910) 15 Am. & Eng. Ann. Cas. 271.

[49]Medford v. Frazier, 58 Miss. 241 (1880). In a bill filed by tenants in common for the partition of the common estate, the court held that the complainants may claim an account for rents received by a defendant cotenant who has been in possession of the common property, but that the tenant in possession will be liable only where it is shown that he has occupied more than his rightful share of the common estate, and then only for the rent of the excess.

[50]Zeigler v. Brenneman, 237 Ill. 15, 86 N.E. 597 (1908); Gulf Refining Co. v. Carroll, 145 La. 299, 82 So. 277 (1919); Pyle v. Henderson, 65 W. Va. 39, 63 S.E. 762 (1909); Williamson v. Jones, 43 W. Va. 526, 27 S.E. 411, 38 L.R.A. 694 (1897); 1 Summers, Oil and Gas (Perm. ed. 1938) § 37; Walker, *Fee Simple Ownership of Oil and Gas in Texas* (1928) 6 Tex. L. Rev. 125, 144 *et. seq.*

The question, then, arises as to whether or not an exception should be made to the general rules of property regarding waste so as to allow one cotenant to produce oil and gas without obtaining the consent of the other cotenants.

The question of the rights of one cotenant to drill or confer that privilege on a stranger without the consent of the other cotenants arises in two situations: (1) Where the common property is land itself, not subject to any oil and gas lease; and (2) Where the common property is the separate mineral interest in a tract of land. In the second situation a cotenant may enjoy his interest only by the removal of the oil and gas. In such a situation then, there seems to be good reason to say that the extraction of the oil and gas amounts to *use* and not *destruction* of the property.[51] Viewed in this light, such extraction does not constitute waste; and a cotenant of a separate mineral interest should not be prohibited from drilling and producing without the consent of the others. Actually, however, the courts do not attach much significance to the distinction between the two situations in determining the rights of the cotenants *inter sese*.

The first case recognizing an exception to the general rules of waste was the Texas case of *Burnham v. Hardy Oil Co.*[52] In that case the court considered the possibility of drainage of the cotenants' oil if one of them refused to join in drilling, and said that since partition in kind was not available for such land, one cotenant alone could drill for and produce oil and gas, being accountable, however, to the others for the value of their proportionate shares, less the reasonable and necessary costs of production.[53] A majority of the jurisdictions have reached a similar result, but have not regarded as important the availability of a right to partition of oil and gas property in kind.[54]

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[51]In Prairie Oil & Gas Co. v. Allen, 2 F.(2d) 566, 571 (C.C.A. 8th, 1924) the court said, "They [tenants in common] may make such reasonable use of the community property as is necessary to enjoy the benefit and value of such ownership. Since an estate of a cotenant in a mine or oil well can only be enjoyed by removing the products thereof, the taking of minerals from a mine and the extraction of oil from an oil well are the use and not the destruction of the estate." See also Dabney-Johnston Oil Corp. v. Walden, 4 Cal.(2d) 637, 52 P.(2d) 237 (1935).

[52]147 S.W. 330 (Tex. Civ. App. 1912), *aff'd*, 108 Tex. 55, 195 S.W. 1139 (1917).

[53]By the passage of Art. 6082, Tex. Stat. (Vernon, 1936), expressly allowing partition in kind of mineral property in Texas, it would seem that one of the main bases for this view has been removed. In this connection see Henderson v. Chesley, 273 S.W. 299 (Tex. Civ. App. 1925), *aff'd*, 116 Tex. 355, 292 S.W. 156 (1927) upholding a partition in kind under the statute; and Rolls v. Wood, 291 S.W. 532 (Tex. Comm. App. 1927) holding that a lease by a cotenant of his interest in oil and gas was not void regardless of whether or not the land could be partitioned.

[54]Prairie Oil & Gas Co. v. Allen, 2 F.(2d) 566 (C.C.A. 8th, 1924); Dabney-Johnston Oil Corp. v. Walden, 4 Cal.(2d) 637, 52 P.(2d) 237 (1935); New Domain Oil & Gas Co. v. McKinney, 188 Ky. 183, 221 S.W. 245 (1920); Hochsprung v. Stevenson, 82 Mont. 222, 266 Pac. 406 (1928); Earp v. Mid-Continent Petroleum Corp., 167 Okla. 86, 27 P.(2d) 855 (1933).

The contrary view is that only upon a showing of actual drainage can a cotenant drill himself or confer that privilege on a stranger without the consent or joinder of all the other cotenants. This view is well set forth in the West Virginia case of *Law v. Heck*.[55] The court there took the attitude that a cotenant in oil and gas was the owner of real estate or an interest therein and that as such he was entitled to have it remain in such condition as he sees fit; that to allow one cotenant to drill without the consent of the others would be to compel the dissenting tenants to exchange real estate for personal property. Several other cases have reached a somewhat similar result.[56]

If partition in kind is available to a cotenant (as apparently it was not in *Law v. Heck)*, this view seems to be the sounder one and the one under which the least amount of confusion will result. It makes an exception to the general rules of waste only where one is absolutely necessary, i.e. where drainage is actually occuring.

However, in view of a holding in Mississippi[57] that it is "self-evident" that deposits of mineral are not susceptible of partition in kind, the reasoning of *Burnham v. Hardy Oil Co.*[58] might well be applied, and it would seem to be most desirable to allow one or more cotenants to drill or to confer that right on a lessee, without the consent of the others.

By way of summary, the following conclusions may be drawn: (1) Whether the courts refer to the extraction of oil and gas by a cotenant without the consent of the others as constituting waste or as mere user, the same result is reached if production is actually obtained — the dissenting cotenants are entitled to their proportion of the value of the oil removed less the reasonable and necessary costs of production.[59] (2) In the jurisdictions regarding such extraction as waste, an injunction may be obtained by the non-consenting cotenants prohibiting drilling by the cotenant himself or his lessee.[60] (3) Though the courts have not regarded the availability of a right to partition of oil and gas property in kind as being important in determining a cotenant's right to extract oil and gas from the common property without the consent of the others, there seems to be good reason for allowing such right of extraction only when partition in kind is not available.

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[55]106 W. Va. 296, 145 S.E. 601 (1928).

[56]Zeigler v. Brenneman, 237 Ill. 15, 86 N.E. 597 (1908); Gulf Refining Co. v. Carroll, 145 La. 299, 82 So. 277 (1919).

[57]Stern v. Great Southern Land Co., 148 Miss. 649, 114 So. 739 (1927).

[58]147 S.W. 330 (Tex. Civ. App. 1912), *aff'd*, 108 Tex. 55, 195 S.W. 1139 (1917).

[59]For cases in which the courts regard such extraction as waste see Martel v. Jennings-Heywood Oil Syndicate, 114 La. 351, 38 So. 253 (1905); Smith v. United Fuel Gas Co., 113 W. Va. 178, 166 S.E. 533 (1932); Williamson v. Jones, 43 W. Va. 562, 27 S.E. 411, 38 L.R.A. 694 (1897). For cases in which the courts regard such extraction as user see Prairie Oil & Gas Co. v. Allen, 2 F.(2d) 566 (C.C.A. 8th, 1924); Dabney-Johnson Oil Corp. v. Walden, 4 Cal.(2d) 637, 52 P.(2d) 237 (1935). In a number of cases the courts do not talk either in terms of waste or in terms of user.

[60]Gulf Refining Co. v. Carroll, 145 La. 299, 82 So. 277 (1919); Law v. Heck Oil Co., 106 W. Va. 296, 145 S.E. 601 (1928).

5. *Leases of Homesteads*

In all jurisdictions having homestead statutes, the courts, when confronted with the problem, have held that the execution of an oil and gas lease by only the husband or wife is within the prohibition of these statutes.[61]

The homestead statutes in Mississippi[62] provide that "A conveyance, mortgage, deed of trust, or other incumbrance . . . shall not be valid and binding . . ." unless signed by both spouses. In view of holdings in Mississippi that the execution of a timber deed,[63] or of a deed granting a right of way across a homestead,[64] comes within the prohibition of the homestead statutes, and in view of a statement by the Court to the effect that the homestead statutes which inhibit the conveyance of the entire homestead by the owner inhibit the conveyance of any part of it,[65] it may be safely prophesied that the Mississippi court will hold that oil and gas leases of homestead property must be signed by both husband and wife.[66]

The question then arises as to the effect of an oil and gas lease executed without the necessary joinder of both husband and wife. It has been held by the Texas court[67] that a lease of homestead property by a husband, not joined in by his wife, is merely inoperative for such time as the property continues to be homestead, or until the lease is ratified by the wife. There are no Mississippi cases involving the validity of oil and gas leases executed without the joinder of both spouses. However, the present Mississippi view seems to be that an instrument conveying any interest in homestead property is absolutely *void* unless signed by both husband and wife. A decision to this effect was announced in the early case of *Cummings v. Busby*.[68] In that case the husband alone had executed a deed of trust on the homestead to secure payment of a debt. The husband and wife then moved off the land, and, the debt not having been paid, the land was bought in by the creditor at a trustee's sale. The husband and wife then brought an action of ejectment against the creditor.

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[61] 1 SUMMERS, OIL AND GAS (Perm. ed. 1938) 9 § 217.

[62] MISS. CODE ANN. (1930) §§ 1778, 1779.

[63] Bruce v. Spears, 181 Miss. 786, 181 So. 333 (1938); Young v. Ashley, 123 Miss. 693, 86 So. 458 (1920); McKenzie v. Shows, 70 Miss 388, 12 So. 336 (1892).

[64] Gulf & S.I.R.R. Co. v. Singleterry, 78 Miss. 772, 29 So. 754 (1901).

[65] In Gulf & S.I.R.R. Co. v. Singleterry, 78 Miss. 772, 777, 29 So. 754, 755 (1901) the court held that a deed of a right of way was a conveyance of an "interest in land," and that "The statute which inhibits the conveyance of the entire homestead by the owner inhibits the conveyance of any part of it, for the whole includes all its parts; otherwise, the statute would be rendered ineffective by construction."

[66] Compare the cases holding that a turpentine lease is not a conveyance of a part of the homestead. Jones v. Adams, 104 Miss. 397, 61 So. 420 (1913); Hancock County v. Naval Stores Co., 93 Miss. 822, 47 So. 177 (1908); Orrell v. Bay Mfg. Co., 83 Miss. 800, 36 So. 561 (1904); Milliking v. Carmichael, 139 Ala. 226, 35 So. 706 (1903).

[67] Grissom v. Anderson, 125 Tex. 26, 79 S.W.(2d) 619 (1935). In that case, the wife who had failed to join in the execution of the lease joined with her husband in the execution of royalty deeds. The court held that the execution of royalty deeds amounted to a ratification of the lease.

[68] 62 Miss. 195 (1884).

The attorneys for the creditor urged that the deed was merely voidable, not void, and that the wife had manifested her consent to waive her homestead rights by an abandonment of the home. The court, in holding that the deed was absolutely void, said, "The deed of trust executed by Busby without the joinder of his wife as required by the statute, was not valid, and its invalidity was not cured by the subsequent removal from the homestead, whether such removal was temporary or permanent. The validity or invalidity of the deed of trust was determinable by the conditions existing when it was executed, and not by what occurred afterward."[69] The decision in *Cummings v. Busby* was cited with approval in a case decided 22 years later in 1906.[70]

In *Young v. Ashley*[71] the husband alone had executed to the defendant a deed to the standing timber on the homestead. Later, he and his wife joined in bringing suit to enjoin defendant from cutting the timber, making no tender of the purchase money received for the execution of the deed. The court said, "We think the principle has been fully settled that the maxim that 'he who seeks equity must do equity' does not apply to a suit to protect the homestead where there is no valid contract. The fact that the husband may have received money for this worthless paper does not prevent him from protecting the homestead."[72] The rule that a conveyance of any interest in the homestead without the signature of both spouses is utterly void has been applied in other cases.[73]

It may be safely concluded, then, that unless there is a departure from the present rule, an oil and gas lease of homestead property in Mississippi, which is executed by the husband or wife alone, will be considered absolutely void, and that such a lease cannot be cured by subsequent ratification by the non-joining spouse or by abandonment of the premises as a homestead.

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[69] *Id.* at 197.

[70] McDonald v. Sanford, 88 Miss. 633, 41 So. 369 (1906). In this case the husband put up the homestead as security for a note executed by him. The husband failed to pay the note and brought suit to recover the homestead. The court said, "The plain purpose of our statute on this subject was to protect the wife in the shelter and refuge of a homestead, unless she has herself joined in conveying away the homestead, and whatsoever name her right may be designated, it is perfectly manifest that no conveyance or mortgage of the homestead, without her joining in the conveyance, is anything less than utterly void." *Id.* at 639, 41 So. at 370.

[71] 123 Miss. 693, 86 So. 458 (1920).

[72] *Id.* at 701, 86 So. at 459.

[73] In Gulf & S.I.R.R. Co. v. Singleterry, 78 Miss. 772, 778, 29 So. 754, 755 (1901) it was said, "Here the conveyance of the husband only was a nullity. . . . The statute makes the homestead community property or clothes it with the incidents of community property, and the signature of the spouse in whom the title is invested without the signature of the other, is inoperative and void." See also McKenzie v. Shows, 70 Miss. 388, 12 So. 336 (1892); Bolen v. Lily, 85 Miss. 344, 37 So. 811 (1904) (The husband, who had executed the deed to the homestead without his wife's joinder, was allowed to recover the land even though he and his wife had later moved off the land and even though his wife had died prior to the commencement of the action); Bruce v. Spears, 181 Miss. 786, 181 So. 333 (1938) (There had been no formal declaration as to what land constituted the homestead).

6. *Leases by Persons Acting Under Powers*

It is a general rule of construction that when a power of attorney is given, the donee of the power is limited very strictly to the quantum of power granted as determined by a strict interpretation of the instrument granting it.

In *Phelps v. Harris,*[74] the earliest Mississippi case involving the construction of the gift of a power, the court seems to indicate a relaxation of the strict application of the general rule. In that case the court upheld a partition made by one Henry W. Vick, under a power conferred by a deed from his wife to "sell and exchange" the property. The court said, "The power to exchange must be understood to include the power of conveying an undivided interest in the whole of the estate in return for a sole or separate interest in a divided part of the estate, or in other words to make a partition. And although a power of sale does not authorize a partition, yet it is believed that a power of exchange is well executed by a partition."[75]

Two later cases, however, indicate that Mississippi will follow the general view. In *Stokes v. Payne, Kennedy & Co.,*[76] the testator empowered another to "sell and dispose of any of the property hereby bequeathed in this will, when it shall appear to him to be advisable so to do, having an eye to the support and education of the children." The court held that this did not outhorize the donee of the power to mortgage the property. In *Columbus Insurance & Banking Co.* v. *Humphries,*[77] a testator by his will conferred on his executors the power to wind up and settle his estate and to sell any of it. The executors, acting under this power, exchanged some shares of bank stock for some bonds. The court held that while the executor had the power to sell the personal estate, as conferred by the will, prima facie, he did not possess the power to exchange one sort of property for another.

Though there are no Mississippi cases involving oil and gas leases executed under a power, cases in other jurisdictions indicate that the same strict rules of interpretation are applicable.[78] In the Texas case of *Bean v. Bean,*[79] Carlos Bean executed a power of attorney to his brother, Nathaniel, giving him the right to "bargain, grant, sell and convey . . . the above described land." Nathaniel, purporting to exercise the power, executed an oil and gas lease which Carlos contended was void because not executed within the power conferred. Even in the face of the Texas view that an oil and gas lease operates as a conveyance of a part of the land, the court upheld Carlos' contention. The court justified its holding on

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[74]51 Miss. 789 (1875).
[75]*Id.* at 793.
[76]58 Miss. 614 (1881).
[77]64 Miss. 258 (1886).
[78]Ohio Oil Co. v. Daughetee, 240 Ill. 361, 88 N.E. 818, 36 L.R.A. (N.S.) 1108 (1909); Lanyon Zinc Co. v. Freeman, 68 Kan. 691, 75 Pac. 995 (1904); Bean v. Bean, 79 S.W.(2d) 652 (Tex. Civ. App. 1935).
[79]79 S.W.(2d) 652 (Tex. Civ. App. 1935).

the ground that it was not within the intention of the parties that the donee should have the power to execute an oil and gas lease. An oil and gas lease being what it is in Texas, namely a conveyance of separate corporeal estate, the same line of reasoning would seem to result in the conclusion that Nathaniel did not have the power to convey a part of the acreage of the land described in the instrument. Whether such a decision effectuates the intention of the parties may be seriously doubted. In view of the holding in *Stokely v. State*[80] that an oil and gas lease in Mississippi is a conveyance of the oil and gas in place, the Mississippi courts may be confronted with a similar problem of interpretation. The more logical holding would be to include the power to execute an oil and gas lease within the power to sell land.

7. Leases of Public Lands

The power to execute an oil and gas lease on state-owned lands is vested in the State Mineral Lease Commission, which was created for the purpose of conserving and protecting the natural resources in or under the public lands of the State of Mississippi.[81] The power of this commission seems to extend to "all of the State land owned now or hereafter acquired by the State, excepting, however, sixteenth section school land, lieu lands and such forfeited tax land and property, the title to which is subject to any lawful redemption. . . ."[82] Apparently however, the power of this commission was not intended to include lands owned by the state which had been previously placed under the control of some other agency.[83]

By statute[84] in Mississippi the boards of supervisors, upon approval of the governor and attorney-general are empowered to lease 16th section lands and lieu lands of their respective counties "for oil, gas, and mineral exploration and development, upon such terms and conditions and for

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[80]149 Miss. 435, 115 So. 563 (1928).

[81]Miss. Code Ann. (Supp. 1938) § 1769 (Miss. Laws 1932, c. 114, as amended by Miss. Laws 1936, c. 191).

[82]Miss. Code Ann. (Supp. 1938) § 1770 (Miss. Laws 1932, c. 114). The exception of "forfeited tax land and property, the title to which is subject to any lawful redemption" from the operation of this statute apparently indicates that no *presently* effective lease could be executed on these lands, the original landowner having been divested of his title by the tax sale, and authority having been given to no agency to execute a lease on behalf of the state.

[83]There are a number of public institutions which may be considered agencies controlling particular lands. In Miss. Laws 1896, c. 117, for example, power is given to the Board of Trustees of the University of Mississippi to sell and lease the land held by the state for the benefit of the University. Under a recent ruling from the Attorney General based upon this act, the Board of Trustees of State Institutions of Higher Learning, successor to Board of Trustees of the University, was advised that an oil and gas lease on University lands could be executed by such board and that it would be unnecessary for the State Mineral Lease Commission to approve of or join in such lease. *Quaere:* Is the power given to the Board of Trustees by the 1896 act now exclusive?

[84]Miss. Code Ann. (1930) § 6762.

such consideration as the board of supervisors, in its discretion, shall deem proper and advisable."

In the case of *Gulf Refining Co. v. Terry*[85] it was held that oil and gas lessees under the above-mentioned statute did not have the right to enter upon 16th section land where there was a lessee holding under a previously made, unexpired lease of the surface for agricultural purposes. This case apparently confines the board of supervisors to the execution of oil and gas leases on 16th section land or lieu lands only if it is not under lease for any other purpose, unless the board or the oil and gas lessee is able to get the lessee in possession to sign a tenant's consent agreement, giving the oil and gas lessee the right to enter for the purpose of oil and gas exploration and development.

Section 211 of the Mississippi Constitution of 1890 prohibits the sale of 16th section and lieu lands. The effect of the holding of the case of *Stokely v. State*[86] is to make the execution of an oil and gas lease a *sale* of the oil and gas.[87] At first glance, then, it would seem that the statute empowering the board of supervisors to execute oil and gas leases on 16th section and lieu lands violates the provisions of the Constitution. However, the court held in the case of *Dantzler Lumber Co. v. State*[88] that a statute authorizing the sale of timber on 16th section land was not violative of the Constitution since the word "land" as used in Section 211 of the Constitution was not intended to have its common law meaning but was only intended to mean the soil itself. Since it is highly desirable to uphold the power of the board of supervisors to execute oil and gas leases in order to enable the schools to realize the utmost out of the land set aside for them, it is probable that the court, when confronted with the question of the constitutionality of the legislative act, will follow the reasoning used in the *Dantzler* case, and will hold the act constitutional.

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[85]163 Miss. 869, 142 So. 457 (1932).
[86]149 Miss. 435, 115 So. 563 (1928).
[87]*Id.* at 447, 115 So. at 566.
[88]97 Miss. 355, 53 So. 1 (1911).